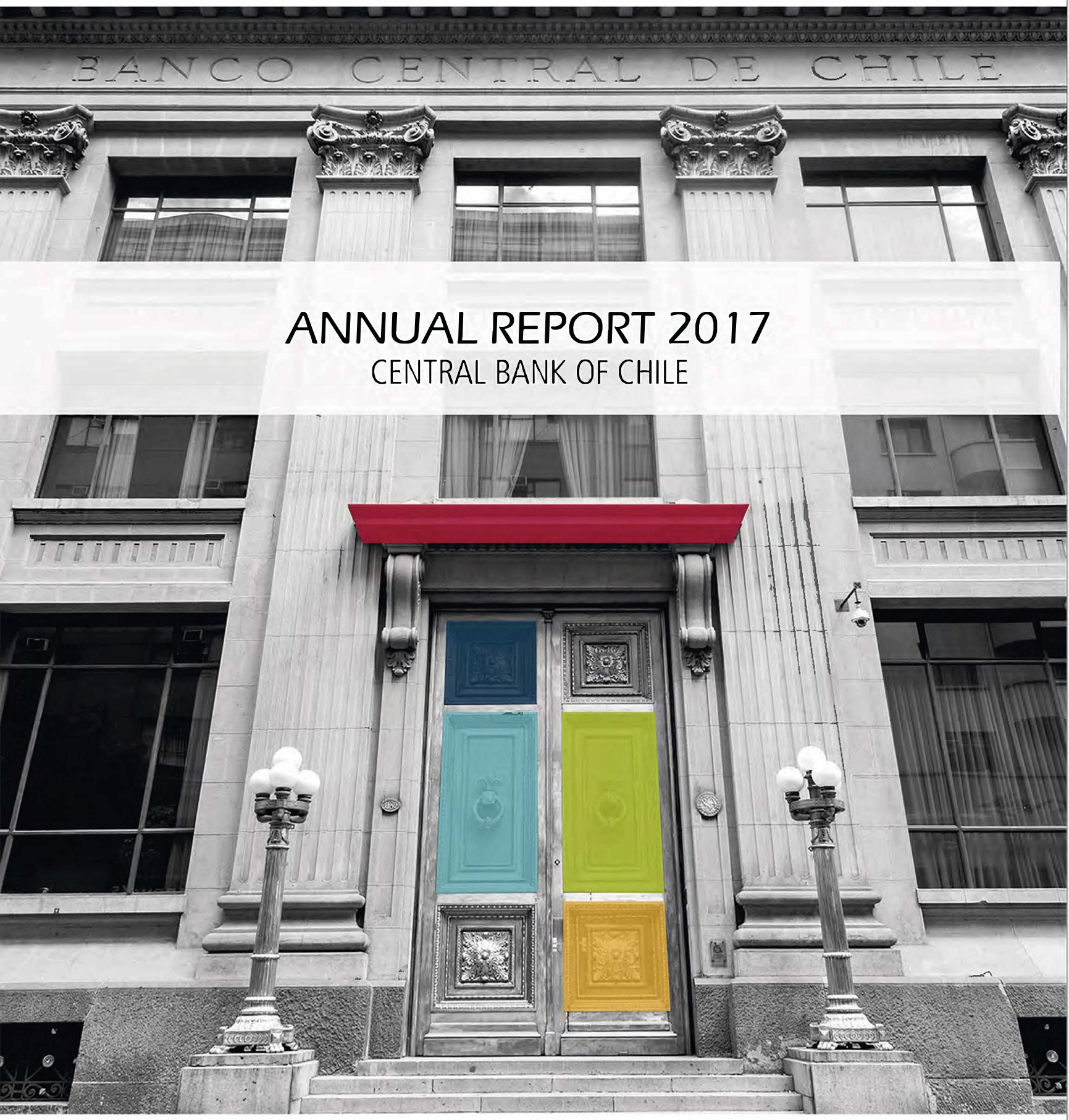

ANNUAL REPORT 2017

CENTRAL BANK OF CHILE

ANNUAL REPORT 2017

CENTRAL BANK OF CHILE

analytical capacity

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intellectual leadership

risk assessment

implementation of legislation

action of financial issues

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SENIOR AUTHORITIES
OF THE CENTRAL BANK OF CHILE
AS OF 31 DECEMBER 2017

Mario Marcel Cullell
Governor

Sebastián Claro Edwards
Deputy Governor (*)

Joaquín Vial Ruiz-Tagle
Board Member

Pablo García Silva
Board Member

Rosanna Costa Costa
Board Member

(*) Sebastián Claro Edwards served as Deputy Governor through Wednesday, 6 December 2017.

AUTHORITIES
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AS OF 31 DECEMBER 2017

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General Manager

Juan Pablo Araya Marco
General Counsel

Silvia Quintard Flehan
Comptroller and Auditor General

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Risk Management

María Inés Urbina De Luiggi
Logistical Services

Claudia Varela Lertora
Institutional Affairs

EMPLOYEE PROFILE

AS OF 31 DECEMBER 2017

452
Men

214
Women

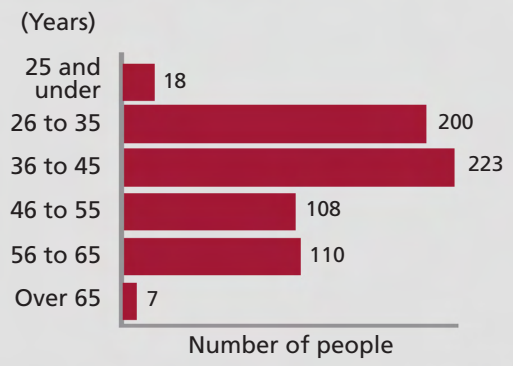
666
Total staff
(Including the four Board Members)

6.3%
Total annual turnover

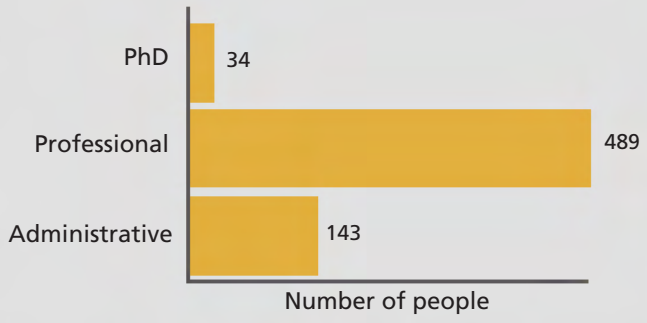
5.2%
Total voluntary turnover

11.2
Average years of service

BY AGE



BY EDUCATION LEVEL



Santiago, 30 April 2018

Mr. Felipe Larraín
Minister of Finance
Santiago

Pursuant to Sections 78 and 79 of the Basic Constitutional Act of the Central Bank of Chile, contained in Article One of Law 18,840, I hereby submit this institution's *Annual Report 2017*.

Sincerely,

MARIO MARCEL
Governor

Santiago, 30 April 2018

Mr. Carlos Montes
President of the Senate
Valparaíso

Pursuant to Sections 78 and 79 of the Basic Constitutional Act of the Central Bank of Chile, contained in Article One of Law 18,840, I hereby submit to the Senate this institution's *Annual Report 2017*.

Sincerely,

MARIO MARCEL
Governor

relation with focus groups

institutional trust

positioning

Communication strategy

feedback mechanisms

effectiveness of communications

CHAPTER 1

1. FINANCIAL MANAGEMENT AND POLICIES OF THE CENTRAL BANK OF CHILE IN 2017

A. ECONOMIC OVERVIEW

Annual inflation was under 3% throughout 2017, averaging 2.2% in the year. The downward trend that started the previous year sharpened considerably, as goods inflation incorporated the effects of the accumulated peso appreciation and the widening of the output gap. Core inflation (CPIEFE) was somewhat lower than headline inflation (2% average in the year). These general trends in inflationary dynamics were amplified by some one-off shocks to volatile prices, most notably fresh fruits and vegetables, where inflation was significantly below the historical average. Energy prices also lowered annual inflation in some months.

On the output side, the year was marked by a low economic performance in the first half of 2017, with some improvement in the second half. Thus, the economy grew 1.5% in annual terms, a little higher than in 2016. Mining output contracted around mid-year, due to the strike at *La Escondida* mine and the slow recovery of mining production in general. In those months, non-mining output recorded limited growth, as a result of one-off shocks in some industrial sectors and fewer business days. The annual GDP growth rate picked up in the second half of the year, supported by an improvement in some of the determinants of domestic spending, in particular business and consumer expectations, and very favorable financial conditions. Domestic spending, excluding inventories, grew 1.9% in the year (2.1% in 2016), driven by consumption. Investment continued to contract in 2017, largely due to construction and works, although there were signs of improvement toward year-end. At the same time, the machinery and equipment component recorded a better performance in the second half of the year. Imports recovered in 2017, especially in terms of consumer goods. The labor market was stable over the course of the year, after deteriorating somewhat in early 2017, especially in wage job creation. Private wage job creation continued to stagnate.

Internationally, the scenario improved during the year. The world growth rate was higher than in 2016 and even exceeded the forecast at the start of the year. The developed world saw the consolidation of a more synchronized recovery in 2017, driven by increased growth in the manufacturing sector, investment-related sectors, and, in the case of Europe, the external sector. Inflation was low in the developed world, with narrowing output gaps and improved labor markets. Headline inflation increased in early 2017, largely due to the annualized increase in energy prices, while core inflation and its forecast remained low. Consequently, the process of withdrawing the monetary stimulus continued to be implemented gradually. In the United States, the Federal Reserve raised the federal funds rate at three of its meetings and initiated a gradual balance sheet reduction process in the fourth quarter. Other central banks, including the United Kingdom and Canada, began their rate hike cycle in 2017. In the Eurozone, the discussion continued on the central bank's market exit strategy, and in the second half of the year the ECB announced that it would reduce its asset purchases starting in 2018. None of these monetary policy actions triggered any major disruptions in the international financial markets.

In this context, global financial conditions remained favorable and were marked by a growing risk appetite. World stock markets rose significantly in the year, recording historical peaks in a number of countries. Emerging markets saw lower spreads, stronger capital flows, and a general strengthening of emerging currencies against the dollar. The peso opened the year at Ch$670 to the U.S. dollar and closed at Ch$615. The peso trend coincided with a significant improvement in the copper price, which rose from US$2.50 to US$3.20 a pound over the course of the year. Other commodity prices also improved in the year. In the case of oil, this was most evident in the second half of 2017. The commodity price trend reflects a better output performance in the emerging world, with China ending the year with a higher growth rate than in 2016.

B. MONETARY POLICY

In 2017, the Board implemented a more expansionary monetary policy, lowering the monetary policy rate (MPR) from 3.5 to 2.5% between January and May. Starting in June, the Board held the MPR at 2.5%, with an expansionary bias. The increase in the monetary stimulus was sooner and much larger in magnitude than predicted by the Board at the start of the year, when the available data pointed to a heightened risk of a widening output gap, which could affect convergence to the inflation target given the low economic growth and the deterioration of some labor market indicators, in particular job creation. In the second half of the year, although inflation remained low and the short-term outlook had decreased in line with the peso appreciation, inflation expectations two years ahead were still around 3%, consistent with a scenario in which the gradual closing of the output gap would help bring inflation back to 3%. In this scenario, the Board weighed the option of new rate cuts, but decided to keep the MPR at 2.5%.

C. FOREIGN EXCHANGE POLICY

Since September 1999, the Central Bank of Chile has applied a floating exchange rate regime, in which the exchange rate is determined by the market. This regime allows for the conduct of an independent monetary policy, facilitates the economy's adjustment to shocks, and prevents large exchange rate misalignments, thereby avoiding a more costly adjustment in terms of output variability and, in principle, attenuating speculative capital flows. Under this floating exchange rate regime, the Bank reserves the option to buy or sell on the foreign exchange market either to adjust its international liquidity position or in the event of an overreaction of the exchange rate, which could potentially have adverse effects. The exchange rate is said to overreact when, without much variation in its fundamentals, it rises or falls sharply within a short period, possibly followed by movements in the opposite direction. The adverse effects of this fluctuation include a loss of confidence among economic agents, stemming from inflationary effects requiring monetary policy measures that are inadequate given the economic cycle, an increase in the volatility in the financial markets, and misleading price signals that may interfere with the efficient allocation of resources.

No such exceptional situations occurred in 2017, and the floating exchange rate regime operated normally, as has been the case for the last six years.

D. FINANCIAL REGULATIONS

In January 2017, the Ministry of Finance, the Central Bank of Chile, the Superintendence of Banks and Financial Institutions, the Superintendence of Securities and Insurance, and the Superintendence of Pensions signed a joint commitment to apply the Principles for Financial Market Infrastructures (PFMI) in their policies, regulations, and supervisory procedures, while also moving forward on gradually eliminating any gaps in their application.

Also in January, the Board approved modifications to Chapter XIV of the Central Bank's *Compendium of Foreign Exchange Regulations* and to Chapters I and XIV of the *Compendium's Procedures and Forms Manual*, to facilitate the operation of international custodians in the country. The changes, which take into account the general orientation of the government's economic policy and safeguard compliance with foreign exchange regulations, have to do with the foreign exchange information required on overseas investments channeled through these custodians.

In March, the Board approved the modification of Chapter III.F.6 of the Central Bank's *Compendium of Financial Regulations* to increase the overseas investment limit for insurance and reinsurance companies, from 20 to 30% of their technical reserves and risk-based capital, via two successive increases of 5% each on 1 March and 1 September. This change was implemented under the framework of Law 20,956, which established measures to boost productivity.

In April 2017, the Board authorized the brokerage firm *MCC S.A. Corredores de Bolsa* to operate in the formal exchange market.

In May, the Board revoked the authorization of the brokerage firm *GBM Corredores de Bolsa Limitada* to operate in the formal exchange market, at the company's request.

In June, the Board approved the new regulations on the issue and operation of credit, debit, and prepaid debit cards, which fully replace Section J of the *Compendium of Financial Regulations*. The changes represent a comprehensive and systematic revision of the regulations on payment cards, in order to incorporate recent developments in this market while safeguarding the security and efficiency of the payment systems. The changes also contain the necessary provisions for implementing Law 20,950, which authorizes nonbank entities to issue and operate prepaid debit cards.

In August, the Board approved the modification of Chapter III.F.3 of the *Compendium of Financial Regulations* with regard to formal secondary markets that are eligible for securities trading by the pension funds. The change expands the category of formal secondary markets to incorporate foreign securities and futures markets located in jurisdictions with a sovereign rating of A or BBB (or the

equivalent) by international credit rating agencies, based on the rating equivalencies established by the Risk Rating Commission under Decree Law 3500 of 1980. These markets must also be on the list of recognized markets maintained by the Superintendence of Securities and Insurance (SVS), in accordance with the applicable regulations (NCG 352).

In October, the Board approved modifications to Chapters III.F.4 and III.F.7 of the Bank's *Compendium of Financial Regulations,* on "Pension Fund Investment Limits" and "Financial Regulations Applicable to the Unemployment Fund Management Corporation, Established under Law 19,728 on Unemployment Insurance," respectively, in order to define the structural investment limits on alternative assets for the pension funds and the Solidarity Unemployment Fund (SUF), in accordance with the provisions of Article 45 of Decree Law 3500 of 1980 and Article 58 B of Law 19,728. Although Law 20,956 allows the Bank to set these limits within a range of 5–15% of the total value of the corresponding fund, the limits were ultimately set below the upper limit of the range for all types of funds. In making this decision, the Board considered that the pension funds' portfolio adjustments should be carried out without affecting the normal functioning of the financial system. Thus, the alternative asset investment limits were set at 10, 8, 6, 5, and 5% for Type A, B, C, D, and E pension funds, respectively, and 5% for the SUF.

Also in October, the Board opened a public consultation on the proposed new Chapter III.D.2 of the Bank's *Compendium of Financial Regulations*, entitled "Recognition and Regulation of Master Agreements for Derivative Contracts." This proposal aims to align the Bank's regulations on the recognition and regulation of master agreements for bilateral derivative contracts with international recommendations and best practices, while safeguarding the financial stability objectives that underlie the Bank's regulations, especially when one of the counterparties is a bank or other institutional investor.

In December, the Board approved the incorporation of a new Chapter III.H in the *Compendium of Financial Regulations* requiring the application of the Principles for Financial Market Infrastructures (PFMI) in the large-value payment systems. This regulation was issued in accordance with the power conferred on the Bank by Article 35 N° 8 of its Basic Constitutional Act. It reflects the commitment assumed in January 2017 by several Chilean regulatory authorities, including the Central Bank, on the application of these principles in their policies, regulations, and supervisory and regulatory procedures.

Also in December, the Bank opened a public consultation on a modification of the *Compendium of Foreign Exchange Regulations* to eliminate the calculation of the reference exchange rate (*dólar acuerdo*) and the associated basket of currencies. This index is not part of the current set of foreign exchange policy instruments, and they have not been used by the Bank for this purpose since the adoption of the floating exchange rate regime in 1999. The proposed measure is in line with the Bank's strategic plan for 2018-2022, which includes modernizing and updating the Bank's foreign exchange regulation, specifically the regulations contained in the *Compendium*.

E. FINANCIAL MANAGEMENT

E.1 Monetary management

To support the implementation of monetary policy, the Bank monitors market liquidity and employs the mechanisms and instruments at its disposal to ensure that the interbank interest rate remains around the monetary policy rate (MPR).

This is achieved through the short- and medium-term liquidity management schedule, which specifies the auction of Central Bank discount promissory notes (PDBC) and bonds (BCP and BCU), as well as other open market operations and standing facilities. In addition, market liquidity forecasts are revised daily and, when necessary, monetary adjustment operations are carried out to facilitate the convergence of the interbank rate to the MPR.

In December 2017, as part of the ongoing modernization of the open market operations system, the Bank incorporated a new collateral-based mechanism for accessing its liquidity facilities, which will operate as a complement to the existing mechanism based on repurchase agreements (repos). Under the new system, General Treasury debt securities (BTP and BTU series) will be accepted as collateral for these operations.

Also in December, extraordinary measures were implemented to facilitate the normal functioning of the foreign currency money market, through eight currency swap auctions totaling US$4.000 billion, based on 28-day contracts and a minimum price of Libor +150 basis points (bp). To offset the effects on liquidity in pesos, a 28-day collateralized repo program was offered through the traditional liquidity window, at a charge rate of MPR + 25 bp.

In 2017, the absolute deviation of the interbank rate from the MPR was zero basis points.

E.2 International reserve management

The purpose of international reserve management is to provide efficient and secure access to international liquidity and to safeguard the financial equity of the Bank. Reserve management is based on the legal framework defined in the Basic Constitutional Act of the Central Bank and on a series of internal policies and practices in line with recommendations from international organizations.

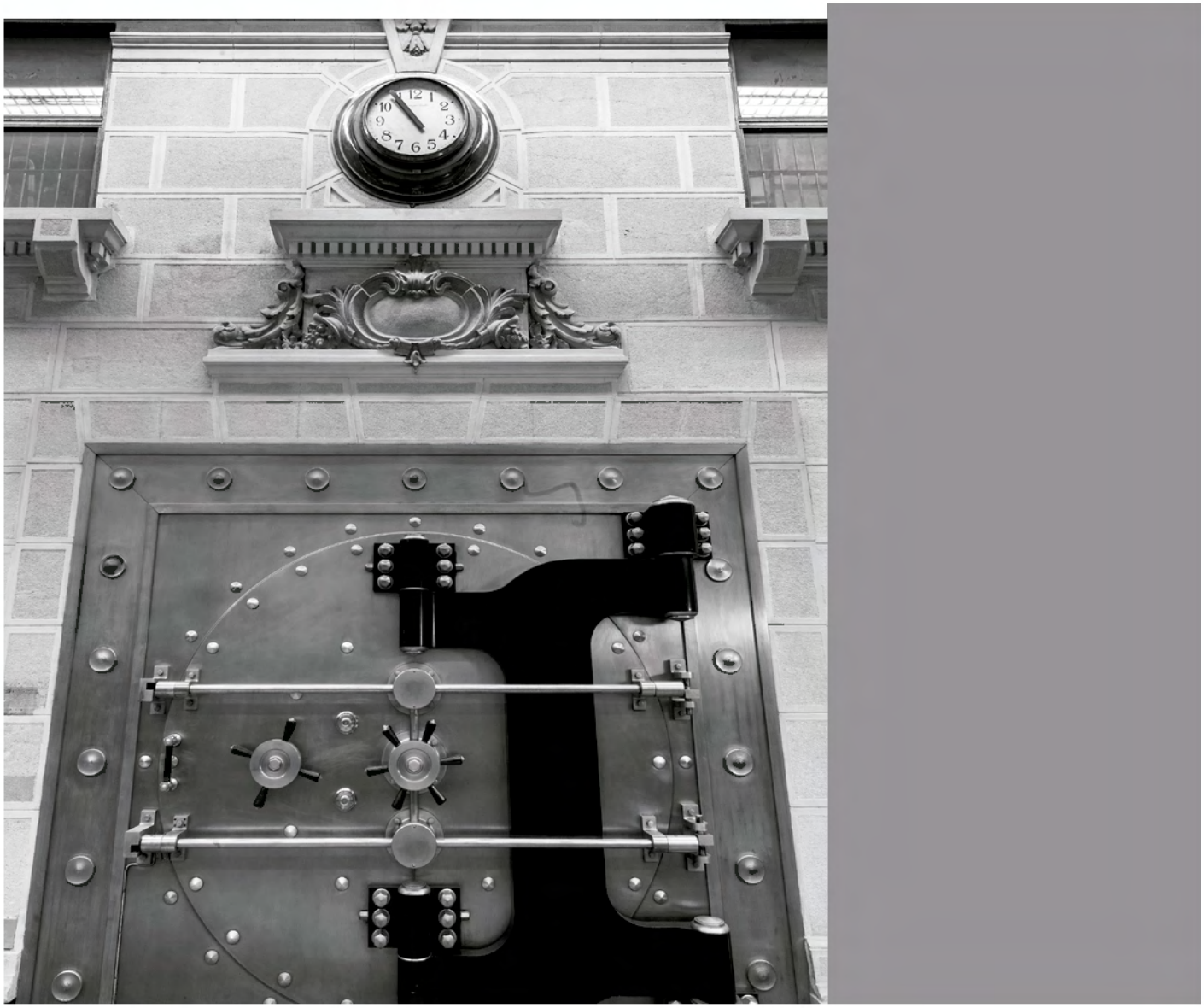
The objectives of the investment policy are as follows: (i) to hold foreign exchange reserves in highly liquid instruments, which can be called in the briefest period possible without incurring significant transaction costs, so as to be able to cover residual short-term external debt if necessary; (ii) to invest in instruments that present limited financial risks, in order to limit the risk of generating capital losses; (iii) to minimize the volatility of the value of the Bank's equity as a result of changes in the exchange rates of the investment currencies vis-à-vis the peso, so as to reduce the negative effects on the Bank's balance sheet; and (iv) to reduce the cost of holding the reserves at the margin, which is achieved through the inclusion of a portfolio oriented toward obtaining higher absolute returns in the long run.

The benchmark structure defines three investment portfolios: (a) the short-term liquidity portfolio (24% of the total reserve investment portfolio); (b) the medium-term liquidity portfolio (61%); and (c) the diversification portfolio (15%). Together, these three funds make up the foreign exchange investment portfolio. The international reserves portfolio further comprises the cash portfolio (transaction account balances held by the General Treasury, public companies, and banks) and the other assets portfolio (IMF special drawing rights, certified gold, and other assets).

In 2017, the Bank held sufficient foreign exchange reserves to meet potential and predictable foreign currency liquidity needs. As of 31 December, the investment portfolio stood at US$35.0710 billion and the cash portfolio at US$2.8770 billion. Taking the sum of these two portfolios plus other assets, international reserves ended the year at US$38.9826 billion. This balance was US$1.5110 billion lower than at year-end 2016. This was explained by a reduction in the cash portfolio of US$3.0795 billion, which was partially offset by increases of US$66.6 million in the other assets portfolio and US$1.5019 billion in the investment portfolio. The increase in the investment portfolio was mainly due to the appreciation vis-à-vis the U.S. dollar of the currencies in which the international reserves are invested, while the increase in the other assets portfolio is explained by IMF transactions. In the case of the cash portfolio, the decrease reflects a reduction in foreign currency deposits by local banks at the Central Bank. In addition, in December, US$30 million was withdrawn from the investment portfolio for the dollar swap program implemented by the Bank.

The liquidity of the reserves was ensured by investing in a portfolio of short-term deposits with international commercial banks and fixed-income instruments traded on highly liquid secondary markets. On 31 December 2017, time deposits and resources held in transaction accounts represented 9.5% of international reserves; short-term securities, 21.5%; bonds, 66.3%; and other assets, 2.7%.

To safeguard the Bank's equity, the invested resources are managed under policies and controls designed to limit financial and operational risk, which are approved by the Board. Credit risk is controlled through limits on issuers, instruments, intermediaries, and custodians. As of 31 December,



77.6% of reserves (excluding other assets) were invested in AAA-rated instruments issued by banks, sovereigns, external financial institutions, or supranationals. The remaining 22.4% was invested in instruments with a credit rating between BBB and AA+, mainly in the sovereign sector. Market risk is limited by diversifying investment currencies, instruments, and maturities. Decisions regarding these parameters always take into account the impact on the Bank's balance sheet.

At year-end, 64.6% of total reserves was held in U.S. dollar instruments, 15.0% in euros, 4.3% in Canadian dollars, 4.3% in Australian dollars, and the remaining 11.9% in other currencies. The average duration of the investment portfolio was around 22 months.

Operational risk was managed through the separation of functions and responsibilities and the application of internal and external controls.

At year-end 2016, a portion of the investment portfolio was managed by two external managers, namely, BlackRock Institutional Trust Company N.A. and Amundi Asset Management. These firms came on board in February and October 2016, respectively, with a mandate of US$500 million each. Both firms manage a long-term global government fixed-income mandate, with a structure equivalent to the internally managed diversification portfolio.

In 2017, the total return obtained from international reserve management was 0.77% measured in currency of origin (not considering changes in the portfolio currencies) and 4.17% measured in U.S. dollars. The return on fixed-income instruments in local currency was offset by the positive exchange rate effect of measuring returns using the U.S. dollar as the base currency. This is due to the depreciation of the dollar against the other currencies in which the international reserves are invested.

The differential return relative to the benchmark (which is used to guide and evaluate investment performance) was 10.8 basis points.

Appendix IV presents a more detailed report, in accordance with institutional policy on the provision of information on the management of international reserves.

E.3 Debt management

The Central Bank's debt management policy is mainly oriented toward having instruments available for the correct implementation of monetary policy, as well as minimizing financing costs. In 2015, the Bank adjusted its debt policy to concentrate on the issue of shorter-term securities of up to five years. This change is in line with international standards in central banking. The new guidelines incorporate a gradual reduction in long-term Central Bank debt.

In early January 2017, the Bank announced its annual bond auction calendar, which considered scheduled debt maturities for an amount equivalent to Ch$1.700 trillion, of which Ch$950 billion would be absorbed through Central Bank discount promissory notes (PDBC).

As in past years, the Central Bank accepted the role of fiscal agent in the placement of General Treasury bonds to be issued during the year. This involved placing UF-denominated General Treasury bonds with maturity dates of 5, 20, and 30 years, which correspond to the reopening of two series issued in 2015 (BTU-5 and BTU-20) and one series issued in 2014 (BTU-30); and peso-denominated General Treasury bonds with maturities of 5, 20, and 30 years, which correspond to the reopening of series issued in 2016 (BTP-5), 2015 (BTP-20), and 2013 (BTP-30). In the year, the Fiscal Agency Decree was modified to transfer the debt service or retirement to the General Treasury or another agent designated for this purpose.

The General Treasury bonds were all issued in accordance with the provisions of Article 104 of the Income Tax Law.

E.4 Provision of large-value payment services

The real-time gross settlement (RTGS) system is the main large-value payment system in Chile and is managed by the Central Bank. Transactions are settled immediately and on a gross basis in the accounts of each bank, in a format that removes credit or liquidity risk, thereby contributing to the stability of the financial system.

At year-end, the number of participants in the RTGS system had fallen to 22, following the anticipated dissolution and consequent revocation of the banking licenses of *Banco París* (January), *Banco Penta* (March), and *Banco Rabobank Chile* (May).

In 2017, the RTGS system settled an average of 1,338 payments per day, including the Bank's own transfers, with an average daily value of Ch$12.17 billion. Relative to 2016, the number of payments was down by 56 per day, while the average value increased Ch$0.53 billion per day. Interbank payments, that is, where the ordering party and the receiving party are both banks, recorded the largest increase in terms of value. In the year, an average of 444 interbank payments were settled per day, with a value of Ch$2.03 billion. On 23 June, the system settled Ch$11.36 billion in payments processed by the banks, the largest amount since 2004.

To increase the efficiency of the RTGS system, the Bank provides liquidity throughout the day via access to an intraday credit facility conditional on the provision of collateral. In November 2017, the Bank modified Chapter 2.3 of the *Compendium of Monetary and Financial Regulations,* which addresses the provision of a line of credit in pesos to banks, backed by collateral. The modification establishes that the Central Bank can grant access to a collateralized line of credit, known as the collateralized intraday liquidity facility, for which banks must sign over sufficient collateral to the Bank. Instruments that are eligible to serve as collateral for this facility are specified in the modified chapter and include bonds issued by the General Treasury of Chile.

In 2017, the intraday credit facility provided an average of Ch$849 billion per day. This represents a strong increase over 2016, when the daily average for the facility was Ch$471 billion. In the year, the largest value provided by the intraday credit facility occurred in June, at Ch$1.96 billion, which was the largest amount recorded since the system was created.

In 2017, the availability of the RTGS system was 100%, while that of the open market operations system, which provides intraday liquidity, was 99.80%. The latter reflects the effect of three incidents that brought the system down for a total of 247 minutes, versus 625 minutes of downtime in 2016.

The Bank participated in a work group created through Chile's Financial Stability Board, aimed at analyzing the operational risks of the payment system and its participants and, if necessary, proposing legal and regulatory changes to mitigate these risks and their effects on the financial system. The Bank also coordinated three business continuity exercises in conjunction with the participants of the large-value payment system and the financial market infrastructures. The goal of these exercises is to ensure that participating organizations regularly test their contingency plans and coordination capacity, identifying opportunities for improvement and sharing experiences that can help improve the resilience of the securities payment and settlement infrastructures.

Finally, in 2017, the Bank maintained its ISO 22301 Certification in Business Continuity Management, including for the RTGS system, following an examination by a registered certification body.

E.5 Management of fiscal funds

Since 2007, at the request of the Ministry of Finance, the Bank has acted as fiscal agent in the management of all or part of the fiscal resources held in the Economic and Social Stabilization Fund (ESSF) and the Pension Reserve Fund (PRF). As of April 2011, the Bank also manages the Strategic Contingency Fund (SCF) in the name of the General Treasury. The Bank submits daily, monthly, quarterly, and annual reports to the to the corresponding government authorities, in accordance with the stipulations of the respective Fiscal Agency Decrees, with measures of performance, risk, and compliance with the specifications in the current performance guidelines.

In 2017, the objective of fiscal fund management was to obtain monthly returns in line with the benchmarks, following the passive management style and risk standards defined by the Finance Ministry in the performance guidelines accepted by the Bank. At the same time, the Bank's management of the funds considered the same standards applied to its international reserve management.

The actual market risk of the ESSF and PRF portfolios, relative to the market risk implicit in the benchmark portfolios established by the Finance Ministry, was primarily controlled through risk budgets (associated with a given ex ante tracking error). Credit risk was mainly controlled through limits on issuers and intermediaries.

At year-end 2017, the ESSF had a market value of US$14.7388 billion, of which US$13.5369 billion was managed directly by the Central Bank[1]/. During the period, the ESSF portfolio managed internally by the Bank received contributions of US$193.0 million[2]/. The PRF had a market value of US$10.0110 billion on 31 December 2017, of which US$6.4243 billion was managed directly by the Bank[3]. In 2017, the PRF received an additional US$333.2 million for management by the Central Bank[4]/.

In 2017, the Bank continued to hire the services of a general custodian, which also measured the performance, risk, and benchmark compliance of the management of the funds, in accordance with the standards and parameters outlined in the performance guidelines.

In 2017, the absolute yield measured in dollars on the funds managed by the Bank was 5.60% for the ESSF and 7.97% for the PRF[5]/. The positive return on the portfolios is mainly explained by the appreciation of the investment currencies vis-à-vis the U.S. dollar.

With regard to fiscal agency fees[6]/, the costs of managing the funds were charged to the General Treasury. In 2017, the annual charges for the ESSF and PRF were 0.7 and 1.6 basis points, respectively, of the total resources under the direct management of the Bank.

In accordance with institutional policy on the provision of information and with specifications in the fiscal agency decree, appendix V presents a more detailed report on the management of the ESSF and PRF fiscal resources.

F. MACROECONOMIC STATISTICS

In 2017, the Central Bank completed its regular macroeconomic statistics revision and publication schedule: National Accounts, Balance of Payments and International Investment Position, Monetary and Financial Statistics, and Foreign Exchange Statistics.

Between March and May, the Statistics Department of the Bank of Portugal conducted an evaluation of the Statistics Division in terms of compliance with statistical best practices, with a focus on the methods and processes used for the compilation and dissemination of the macroeconomic statistics

[1]/ The remaining ESSF resources are managed by external portfolio managers under an equity mandate.
[2]/ The contribution was a transfer from the externally managed equity portfolio, in the context of the annual ESSF portfolio rebalancing on 28 June 2017.
[3]/ The remaining PRF resources are managed by external portfolio managers under corporate bond and equity mandates.
[4]/ This is the net increase from a contribution of US$537.2 million, received on 28 June 2017, and a withdrawal of US$203.9 million, on 13 September 2017.
[5]/ Both figures were obtained using the time-weighted rate of return (TWRR) methodology, which delivers a rate of return adjusted for the impact of possible contributions (of capital or generated by the securities lending program) and withdrawals (of capital or associated with payments to third parties). This methodology thus isolates the management result from the effect of changes that are exogenous to the size of the portfolio, thereby allowing a comparison of the portfolio management and the benchmark performance.
[6]/ The annual fiscal agency fees for the ESSF and PRF are associated with direct expenses and costs incurred by the Bank in the management of the funds and does not consider charges by the external portfolio managers for the management of their respective portfolios.

elaborated by the Division. The resulting report indicates that the statistics generated by the Bank are complete and high quality. The Bank follows internationally accepted standards and best practices, and, in general, the available sources provide an adequate basis for the compilation of macroeconomic statistics. Furthermore, the data solutions used in statistical production are updated periodically to reflect the needs of compilation, while also safeguarding information security.

To maintain the high quality standards of its statistical products, the Bank published the new national accounts series in March, based on the 2013 Benchmark Compilation, which is the statistical infrastructure that provides the basis for the elaboration of the national accounts of the Chilean economy from 2013 onward. The new series incorporate the implementation of methodological innovations derived from international recommendations (such as the incorporation of economic activity and product classifications based on Revision 4 of the International Standard Industrial Classification and Revision 2 of the Central Product Classification; and the capitalization of research and development expense), new sources of information not available in the usual compilation, and the associated methodological changes (most notably, a new measure of the construction sector). The spliced historical series were published in conjunction with the 2016 results.

In May, the Bank published the national accounts series by institutional sector, with the implementation of the methodological standard proposed in the 2008 System of National Accounts (SNA), including an updated classification of institutional sectors and financial instruments and a new measure of production for general insurance companies. In addition, the statistical disaggregation of intersectoral exposures was expanded with the publication of from-whom-to-whom matrices for the following instruments: legal money, debt securities, money market fund shares, and other investment fund shares.

To achieve a more efficient and centralized management of the different internal micro-databases, in 2017 the Bank continued to move forward on the Micro-data: Integration, Development, and Exploitation (MIDE) project, with the centralization and organization of micro-databases, privacy protection, and the use of specialized software available internationally.

Exploring the use of "big data" is a major current issue for central banks. This complex task poses significant operational challenges in terms of data management and creates new information and research needs. Therefore, the Bank's Statistics Division is participating in one of the main initiatives developed by the Irving Fisher Committee (IFC) of the Bank for International Settlements (BIS) in 2017, in which IFC members have been invited to cooperate in sharing their experiences and monitoring developments on big-data-related issues, analytical methodologies, their value compared with "traditional" statistics, and the risks involved in their use, such as the generation of a false sense of certainty and precision. The IFC has focused on a few pilot projects intended to cover four areas: (i) Internet data; (ii) administrative data; (iii) commercial data; and (iv) financial market data.

To address the future demands of central banking in the areas of statistics and financial stability, the Statistics Division is working on the creation of a data repository for derivative transactions, in line with international standards, as well as access to the information by the different regulators. Current tasks

include reviewing the international experience, identifying the information that will be needed by market agents, and creating an electronic platform to facilitate data shipping, storage, and handling.

The Statistics Division participates in several working groups of the Organization for Economic Cooperation and Development (OECD) on macroeconomic and foreign trade statistics, including the Working Party on International Trade in Goods and Trade in Services Statistics, the Working Group on International Investment Statistics, the Working Party on National Accounts, the Working Party on Financial Statistics, the Working Party on the Measurement and Analysis of the Digital Economy, the Working Party of National Experts on Science and Technology Indicators, the Expert Group on Micro statistics on Household Income, Consumption and Wealth, and the Committee on Statistics and Statistical Policy. These groups provide an opportunity to share information, experiences, and perspectives with representatives of advanced economies, as well as access to documentation on international standards and best practices for new data requirements, new statistics, updated methodologies, and the use of new sources.

Finally, in 2017, the use of statistical applications continued to increase, albeit with changes in user preferences. The Daily Indicators web page was still the most used, with 5.6 million visits in the year (Google Analytics); this is in line with the daily frequency of the information provided there. In second place this year was the Statistical Database for mobile devices, which grew from around 400,000 hits in 2016 to over 675,000 in 2017. The traditional Statistical Database received 670,000 visits. Finally, in 2017 the use of the web service, which allows massive data downloads via direct connection between servers, more than doubled, with over 100 companies using this service regularly.

G. TREASURY MANAGEMENT

In 2017, the Treasury Management continued to fulfill its legal mandate to oversee cash cycle management so as to ensure the normal functioning of the payment systems, in particular with regard to cash money in circulation in the country.

As in most countries, cash is still the most commonly used means of payment in Chile in terms of people's preferences, which has systematically been the case over the past several years. Consequently, cash is a critical component in the Central Bank's provision of reliable, secure, and timely payment means, as are commercial banks given their role in the money cycle. Commercial banks play a key role in the cash cycle, since they are the only intermediaries between the Central Bank and the end users of banknotes and coins, namely, trade, businesses, and individuals.

In terms of cash requirements, the Central Bank satisfied virtually all the demand from commercial banks in 2017. This provided the supply for one of the key channels of cash distribution—namely, automatic teller machines (ATMs)—while also meeting the needs of the banks' main clients, including retail and wholesale businesses and the public sector, which are the main sources for people to obtain banknotes and coins.

In 2017, the value of bills and coins in circulation grew 3.7% in annual terms, nearly a full percentage point higher than in 2016 (2.8%). In terms of units, the quantity of banknotes issued in 2017 recovered significantly from a year ago, recording annual growth of 2.2%; this compares very favorably to the practically null growth of 2016 (0.2%). In terms of value, the banknotes issued in 2017 grew 3.5% annually, one percentage point more than the previous year (2.5%). The number of banknotes in circulation reached 967.9 million[7]/ In the same period, the number of coins in circulation grew 3.6%, totaling 14.5687 billion coins in December 2017[8]/,which represents an annual growth rate of 7.6% in terms of value.

As in past years, the $10,000 bill continues to account for the largest share of cash in circulation, at 37%. The largest and smallest denominations, $20,000 and $1,000, increased their shares to 21.9 and 29%, respectively. Thus, these three denominations account for 87.8% of the total banknotes in circulation. The denominations most requested by commercial banks are the two largest banknotes ($20,000 and $10,000), mainly due to their use in ATMs based on the higher logistical efficiency and lower cost for the commercial banking sector. With regard to coins, the $10 is the most requested by commercial banks, and the Bank supplied a total of 356 million or these coins in 2017.

[7]/ The number of banknotes in circulation does not include the category "Other banknotes," which comprises the Ch$100 and Ch$50 peso denominations from the old banknote series.
[8]/ The number of coins in circulation does not include the category "Other coins," which comprises *centavos* and *escudos* issued by, but not returned to the Central Bank of Chile, or commemorative coins issued by the Central Bank of Chile in Ch$10,000 and Ch$2,000 peso denominations.

To satisfy the demand for cash, the Bank distributed new banknotes and coins to commercial banks, following deliveries in 2016 and 2017 of production previously contracted out to suppliers following international tender processes. The banknotes issued in the period were printed in Sweden and Germany; the coins were minted in Holland and Chile.

In 2017, the most important currency-related event was the elimination of the $1 and $5 coins, pursuant to Law 20,956, which modified the set of currency in use in the country and which entered into effect on 1 November 2017. The law authorized the Central Bank to stop issuing these two coins, established a rounding rule for cash payments, and ordered the Bank to withdraw the coins from circulation. To comply with the provisions of the law, the Bank held a tender process for contracting a national publicity campaign to notify the public of the new regulations and to provide information and educational material on the rounding rule.

For this communication, the Bank developed a strategy centered on a press and publicity campaign for reporting on the content and implementation of Law 20,956 in the media, including network and cable television, national and regional newspapers, national and local radio stations, street advertisements, and digital media. The publicity campaign was seen by 99.2% of the target population, and it was rated as useful, informative, and educational by 74% of the target audience. The Bank also set up a website dedicated to providing information and answering questions.

The Bank developed a strategy for withdrawing the $1 y $5 coins from circulation, by providing publically accessible locations for exchanging the coins for larger denominations. These included a special window at the Central Bank building, all branches of the Banco del Estado de Chile nationwide, and other commercial bank branches where the Central Bank has custodian vaults.

By late 2017, the process of recovering the $1 and $5 coins was fully underway and was proceeding as expected. As suggested by the international experience, the recovery rates are fairly low as a percentage of the total $1 and $5 coins issued, which date to 1992. This is due to the low purchasing power and small size of the coins, which contribute to a high loss rate over the course of the years.

A new version of the National Survey on Cash Use and Preferences was carried out in 2017. The results confirm the trend of previous years, where cash continues to be the primary payment means used all across Chile, especially for small-value transactions. This is despite the increased coverage of electronic payment means, which are still used fairly moderately in Chile.

In terms of the distribution of banknotes and coins, the public expressed a high level of satisfaction with the quantity in circulation. The quality of the Chilean bills in circulation is generally perceived to be high, which facilitates their recognition and validation.

With regard to the care and conservation of the banknotes—which is crucial for maintaining their quality and ease of recognition—the survey revealed that the vast majority of people are aware that certain habits can damage the bills.

Logistics center project

The Central Bank has a constitutional mandate to carry out the safe and efficient provision and management of cash in circulation, in order to safeguard the operational continuity of the storage and distribution of cash in the country. To achieve this, the Treasury Management has developed a number of projects over the years aimed at improving its processes and products, so as to guarantee the continuity and quality of the supply of banknotes and coins.

One of the most important projects currently underway is the construction of a new Logistics Center, which began in 2015 with the purchase of a property in the *El Montijo* Industrial Park (in the *Renca* county). The goal of this project is to modernize the Treasury functions, thereby supporting the continuity of the money supply and the efficient execution of the Bank's role as sole issuer of the national currency, based on the highest technological and security standards and best practices in central banking.

Specifically, in 2017 the Bank continued work on the security and communications consulting phases initiated in 2016. A preliminary structural consultant was hired, and the consulting on logistical solutions entered the second phase, aimed at optimizing the Treasury Management's future functional processes. Also in 2017, the Bank contracted the services of an Owner's Engineer, which will provide support on the administration and management of activities pertaining to subsequent phases of the project life cycle, in particular those related to construction and engineering works.

In 2018, a tender process will be held for the basic architectural and engineering design; there will be a second phase of security consulting; and a tender process will be held for the detail engineering.

Modernization of the Treasury Information System (TIS)

The supply of cash to the community is executed through the commercial banks, using computer systems that must be updated periodically. In November 2016, work began on developing a new Treasury Information System (TIS), which went into operation in July 2017.

This initiative was spearheaded by the Treasury Management, with support from different divisions within the Bank as well as an external consultant. The TIS project included substantial participation by the commercial banks and was built using the SAP enterprise resource planning (ERP) system. The new system supports the Bank's cash management processes on a robust platform that is integrated with other systems, automating and optimizing the associated processes, increasing efficiency, and reducing financial and operational risks. The system provides full traceability of the process; visualization, management, and monitoring of banknotes and currencies at all stages and all points of origin; and online information on the cash levels in the custodian vaults throughout the country.

H. THE BALANCE SHEET OF THE CENTRAL BANK OF CHILE

H.1 Balance sheet levels and structure[9]/

The behavior of the economy and the policies adopted by the Central Bank of Chile affect the size and composition of the Bank's balance sheet, which in turn affects the trend in earnings and losses. Thus, the debt in the form of Central Bank promissory notes on the liability side is largely explained by the need to finance the rescue of the financial system following the crisis in the first half of the 1980s and by the need to sterilize the monetary effects of the accumulation of international reserves in the 1990s and, more recently, in 2008 and 2011.

Measured in pesos, the size of total assets decreased by Ch$2.910 trillion in 2017 (table 1.1). Measured relative to GDP, total assets contracted from 16.5 to 13.9% between 2016 and 2017. The largest reduction, of Ch$3.038 trillion, was in the foreign reserves balance. This was due to the appreciation of the peso (-$1.113 trillion), interest earned ($312 billion), and net withdrawals by commercial banks and the General Treasury (–$2.236 trillion). Other significant changes on the asset side include an increase of Ch$291 billion in monetary policy assets (due to repo operations and, to a lesser extent, the standing liquidity facility) and a reduction of Ch$124 billion in subordinated debt due to the payment of the annual quota by the *Banco de Chile.*

[9]/ The balance sheet is prepared in accordance with International Financial Reporting Standards (IFRS). See the Financial Statements (note 2(a)).

TABLE 1.1

CENTRAL BANK OF CHILE BALANCE SHEET

(balance in Ch$ billion and % of GDP, as of 31 December of each year)

	2016		2017		Rate of return (1) (%)			
					2016		2017	
	Balance	GDP%	Balance	GDP%	interest	Δ value	interest	Δ value
Assets	**27,908**	**16.5**	**24,998**	**13.9**	**1.2**	**-7.9**	**1.3**	**-4.3**
International reserves	27,021	16.0	23,983	13.3	1.2	-8.3	1.2	-4.4
Other public sector assets (2)	300	0.2	310	0.2	0.0	2.8	1.6	1.7
Subordinated debt	355	0.2	231	0.1	5.0	2.9	5.0	2.2
Monetary policy instruments (3)	13	0.0	303	0.2	0.9	0.0	1.5	0.0
Other	220	0.1	171	0.1	1.0	5.9	0.8	-10.5
Liabilities	**32,114**	**19.0**	**30,781**	**17.1**	**2.2**	**1.6**	**1.9**	**0.7**
Monetary base	10,342	6.1	11,106	6.2	0.3	0.0	0.2	0.0
Monetary policy promissory notes (4)	15,114	8.9	14,837	8.3	3.9	1.2	3.3	0.7
Other monetary policy liabilities (5)	1,380	0.8	2,269	1.3	2.1	0.7	2.1	0.0
Current accounts and bank foreign currency reserves	3,911	2.3	1,437	0.8	0.0	8.8	0.0	0.3
General Treasury and other public sector deposits	780	0.5	318	0.2	0.6	3.5	1.0	0.5
Other	586	0.3	814	0.5	0.5	6.7	0.7	10.8
Equity	**-4,206**	**-2.5**	**-5,783**	**-3.2**				
Initial capital	-1,984		-4,217					
Valuation accounts (6)	11		17					
Other (6)	0		0					
Net result	-2,233		-1,584					
Non-financial result (7)	-86		-96					
Net interest (7)	-345		-249					
Change in value (8)	-1,801		-1,239					
Capital contributions	0		0					

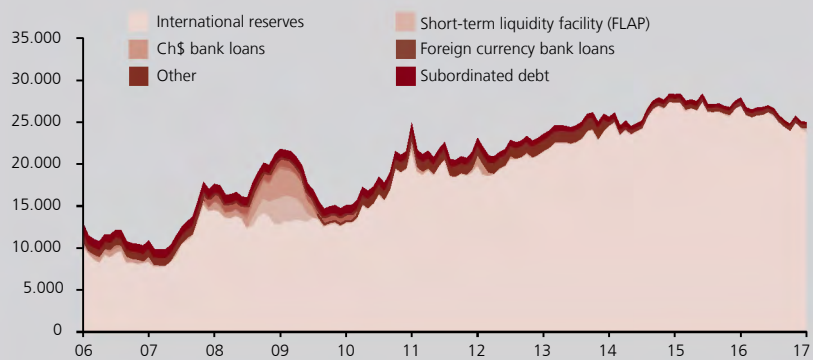
(1) Implicit rates are calculated based on average monthly balances and losses/gains due to interest or changes in value.
(2) Includes a provision for 100% of the "Sinap liquidation" asset for Ch$1.134 trillion in 2016 and Ch$1.211 trillion in 2017.
(3) Includes credit to banks guaranteed with foreign currency deposits (foreign currency swaps) or risk-free securities (repos) and liquidity lines in domestic and foreign currency.
(4) Includes PDBC, BCP, PRC, CERO UF, and BCU.
(5) Short-term remunerated bank deposits in domestic and foreign currency. Foreign currency deposits, except daily deposits, guarantee credits in domestic currency (note 3).
(6) See the Statement of Changes in Equity in the 2017 Financial Statements.
(7) The foreign currency component of these items is converted to pesos using average exchange rates.
(8) Includes price-level restatements in domestic currency and the effect of exchange rate fluctuations on assets and liabilities in foreign currency.

Source: Central Bank of Chile.

Liabilities (excluding equity) decreased Ch$1.333 trillion in 2017, contracting from 19.0 to 17.1% of GDP. The largest reduction was recorded in the current account balance and commercial banks' foreign currency reserves (–$2.474 trillion), followed General Treasury and other public sector deposits (–$462 billion) and monetary policy promissory notes (–$278 billion), due to maturing BCU and BCP bonds. This was partially offset by increases in other monetary policy liabilities ($889 billion), due to greater use of the standing deposit facility; the monetary base ($763 billion); and other liabilities ($228 billion).

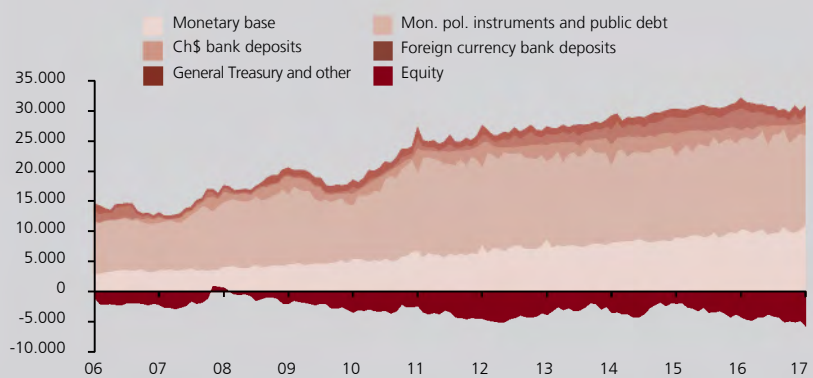
As a result, the Bank's equity deficit increased in 2017, with a larger reduction in the nominal value of assets versus liabilities (figures 1.1 and 1.2). The balance sheet carried negative equity of Ch$5.783 trillion, reflecting initial capital of -$4.217 trillion, other reserves of $17 billion, and a net loss in 2017 of -$1.584 trillion. The latter is explained by a loss of Ch$1.239 trillion from the monetary restatement of assets and liabilities, mainly due to the exchange rate; interest expense of Ch$249 billion; and nonfinancial costs of Ch$96 billion, mostly deriving from the production and distribution of currency and to personnel and administrative expenses.

FIGURE 1.1
CENTRAL BANK OF CHILE ASSETS
(balance as of 31 December, in Ch$ trillion)



Source: Central Bank of Chile.

FIGURE 1.2
CENTRAL BANK OF CHILE LIABILITIES
(balance as of 31 December, in Ch$ trillion)



Source: Central Bank of Chile.

H.2 Return on assets and the cost of liabilities

The average return on assets, mainly reserves, is determined by the level of external interest rates on safe, highly liquid instruments. The cost of liabilities is associated with the MPR and its expected trend, which affects the placement rate for Central Bank promissory notes. In 2017, the differential between the interest earned on assets (1.3%) and the cost of liabilities (1.9%) was negative, at 0.6%.

The average interest rate earned on international reserves was 1.2% between 2016 and 2017, due to low coupon rates on the component instruments. Locally, the interest rate on monetary policy promissory notes decreased 60 basis points, primarily due to an increase in the share of short-term debt made up by PDBC and a corresponding decrease in BCU and BCP, together with the drop in the MPR.

With regard to adjustments, exchange rate fluctuations generated accounting losses in 2017, as did variations in the UF (*unidad de fomento*, an inflation-indexed unit of account). As usual, the biggest contributing factor was the exchange rate effect, given its impact on the value of the international reserves in pesos. Between year-end 2016 and year-end 2017, the peso appreciated against the currencies that make up the foreign exchange reserves, causing the value of the reserves to fall by 4.4% and total assets by 4.3%. At the same time, the effects of lower inflation on UF-denominated notes and of exchange rate fluctuations on current and collateral accounts in foreign currency resulted in an adjustment of 0.7% in the value of total liabilities, which is 0.9 pp less than in 2016.

H.3 Balance sheet positions by currency[10]/

The reduction in the Bank's position denominated and payable in domestic currency is largely explained by negative interest flows and changes in the valuation of the position in domestic currency (—Ch$728 billion), primarily due to the costs of Central Bank promissory notes (table 1.2a).

The position denominated and payable in foreign currency increased US$1.462 billion, mainly due to interest, adjustments, and other flows associated with exchange rate gains (the appreciation of other currencies against the U.S. dollar) and interest on international reserves of US$1.749 billion (table 1.2b).

[10]/ The positions or balances of assets less liabilities by currency can be used to evaluate equity exposure to foreign exchange risk. By disaggregating the changes into flows from (a) exchanges between balances and (b) interest and valuation changes, it is possible to more closely monitor the policies adopted by the Bank.

TABLE 1.2A

CENTRAL BANK OF CHILE BALANCE SHEET POSITIONS

(balance as of 31 December of each year; annual flows in Ch$ billion)

		2017 flows (4)		
	Balance 2016	Exchange (5)	Earnings and Δ capital (6)	Balance 2017
Denominated and payable in pesos (1)	**-26,610**	**0**	**-728**	**-27,338**
Monetary base (2)	-10,342	-743	-20	-11,106
Central Bank promissory notes	-15,114	899	-622	-14,837
Banks	-1,354	-592	-38	-1,984
Other	201	436	-48	588
Denominated in foreign currency and payable in pesos (1)	**0**	**0**	**0**	**0**
Denominated and payable in foreign currency (1)	**22,404**	**0**	**-850**	**21,554**
Equity (1)	**-4,206**	**0**	**-1,577**	**-5,783**

TABLE 1.2B

FOREIGN CURRENCY POSITIONS ON THE CENTRAL BANK BALANCE SHEET

(balance as of 31 December of each year; annual flows in US$ million)

		2017 flows (4)		
	Balance 2016	Exchange (5)	Earnings and Δ capital (6)	Balance 2017
Denominated and payable in foreign currency	**33,572**	**0**	**1,462**	**35,034**
International reserves (3)	40,494	-3,260	1,749	38,983
Central government (net)	-474	-42	0	-517
Banks (net)	-5,481	3,145	0	-2,336
Other (net)	-966	157	-287	-1,096
TOTAL	**33,572**	**0**	**1,462**	**35,034**

(1) The positions are defined as assets minus liabilities, so the difference is equivalent to equity. Because assets are added and liabilities are subtracted, the resulting signs of both balances and flows must be incorporated, with the same sign, as positive or negative contributions to equity.
(2) Because the monetary base is a negative component of the position denominated and payable in domestic currency, its negative flows (due to exchange or net profits) correspond to increases in the position, while positive flows correspond to decreases. Exchange flows of other entries are the balancing entry of its increase or decrease due to exchanges.
(3) Because international reserves are a positive component of the position denominated and payable in foreign currency, flows reflect the direction of its variations (with the same sign). Exchange flows of other entries with the opposite sign are the balancing entry of its increase or decrease due to exchange.
(4) Flows are, in general, the result of operations or imputations that translate into changes in balances.
(5) Exchange flows are produced whenever an asset or liability is modified as a consequence of the opposite variation of another asset or liability. In aggregate terms, exchanges alone do not change the equity level.
(6) Includes interests, price-level restatements, and other changes in value, profits minus nonfinancial losses, and capital contributions.

Source: Central Bank of Chile.

I. Miscellaneous

I.1 Commission on Price Distortions

The National Commission on Price Distortions is in charge of investigating the existence of price distortions on imported goods. It is a technical body composed of representatives from public institutions in the economic sector. Its task is to advise the President of Chile on the application of antidumping measures, countervailing duties, and safeguard measures. The Commission operates independently from the Bank, although the Technical Secretariat resides within the Bank as stipulated in Law 18,525. Its functions include gathering background information for investigations, preparing technical reports, channeling communication among the parties involved, and carrying out pertinent notifications.

The Central Bank Board appoints two members and two alternates to sit on the Commission.

In August 2017, Mr. Marcus Cobb Craddock was appointed as alternate for Mr. Francisco Ruiz Aburto. In October 2017, Mr. Rodrigo Alfaro Arancibia was appointed Commission member; his alternate is Ms. Beatriz Velásquez Ahern.

In 2017, the Technical Secretary provided support services to the Commission on Price Distortions, which met on ten occasions. In the period, the Commission decided to open one investigation and recommended the application of one provisional measure and two definitive measures. At year-end, there were two definitive antidumping duties in effect, for imports of steel wire rods and steel bars, respectively, from China.

I.2 Chilean Copper Commission (Cochilco)

Pursuant to Article 4 of Decree Law 1349 of 1976, the Board is responsible for appointing two representatives to the Chilean Copper Commission, who serve a two-year term.

In 2017, these seats were held by Mr. Miguel Fuentes Díaz and Mr. Francisco Ruiz Aburto. In both cases, the two-year term of office runs through 24 October 2018.

I.3 Competition Tribunal (TDLC)

The Competition Tribunal (*Tribunal de Defensa de la Libre Competencia*, or TDLC) is made up of five Judges and two Alternates[11]/ The President of the Republic appoints the President of the Tribunal, who must be a certified lawyer, choosing from a list of candidates provided by the Supreme Court following a public call for nominees. The Board of the Central Bank is responsible for appointing a Judge / Legal Counsel and a Judge / Economist, as well as an Alternate Judge / Economist, following a public call for nominees. The Board also provides the President of the Republic with a short list for choosing a Judge / Legal Counsel and a Judge / Economist, as well as an Alternate Judge / Legal Counsel, following a public call for nominees.

[11]/ Article 6 of Decree with force of law N° 1, of 2005, issued by the Ministry of Economy, Development, and Reconstruction (DFL N° 1).

Once chosen by the competent authority, the judges are appointed via Executive Decree, issued by the Ministry of Economy, Development, and Tourism and countersigned by the Finance Minister, for a period of six years, with a staggered replacement of judges every two years.

In 2017, the Board was not required to make appointments or proposals for judges or alternates on the Tribunal.

However, through Executive Decree N° 4, of 20 January 2017, published in the *Official Gazette* on 28 April 2017, Mr. Nicolás Sebastián Rojas Covarrubias was appointed Alternate Judge / Legal Counsel, based on the short list proposed by the Board through Resolution 2022E-01-161205.

I.4 Technical Investment Council

The Board is authorized to appoint a member and an alternate to the Technical Investment Council, pursuant to Article 168 of Title XVI of Decree Law 3500 of 1980, on the pension system reform, and Articles 58-E and 58-H of Law 19,728, which establishes mandatory unemployment insurance.

Mr. Rodrigo Cerda Norambuena was appointed by the Bank as Council Member and Ms. Catherine Tornel León as alternate, both for a period of four years starting on 11 June 2016.

I.5 Technical Commission Created under Article 6 of Law 18,480

This Technical Commission is responsible for reviewing applications for reconsideration of the input tax credit for exporters, as stipulated in Article 6 of Law 18,480, which establishes a system for refunding taxes and duties assessed on the cost of inputs for small nontraditional exports.

The members of this Commission will be proposed by the entities they represent and then appointed through a resolution issued by the Ministry of Economy, Development, and Tourism, which must be published in the *Official Gazette*. The Central Bank Board has the capacity to appoint a representative to this Commission, in accordance with the stipulations of Article 6 of the aforementioned law.

Ms. Ivette Alejandra Fernández Delgado is the Bank's current representative on this Commission, with Ms. María Isabel Méndez Ferrada as alternate, per Board Resolution 1937-02-151029.

I.6 Technical Commission Created under Article 4 of Law 18,634

This Technical Commission is responsible for reviewing applications for inclusion or exclusion on a list, established by Finance Ministry Decree, of the capital goods covered under Law 18,634 which sets up a scheme for deferred payment of customs duties, tax credits, and other tax benefits.

The Central Bank Board has the capacity to appoint a representative to this Commission, in accordance with the stipulations of Article 4 of the aforementioned law.

Ms. Ivette Alejandra Fernández Delgado is the Bank's representative on this Commission, with Ms. María Isabel Méndez Ferrada as alternate.

process streamlining

definition of responsibilities

teamwork

collaboration between areas

delegation of authority

comprehensive and balanced vision

accountability

CHAPTER 2

2. INSTITUTIONAL MANAGEMENT AND GOVERNANCE

A. ORGANIZATION AND OPERATION

A.1 The Board

The Board has five Members, one of whom acts as chair and also serves as the Central Bank's Governor. The Board is responsible for the senior governance and management of the Bank, in its quality as an autonomous, technical public institution with constitutional authority. Board Members are appointed by the President of Chile by means of an Executive Decree issued by the Ministry of Finance, with preliminary approval from the Senate. Members hold office for a renewable period of ten years, and the Board is reconstituted on a partial basis every two years, when one member is changed at a time[12]/.

The Bank's Governor is appointed by the President of Chile from among the Board Members. The Governor holds office for five years or until his or her appointment as Board Member expires, whichever comes first, and may be reappointed for new periods. Along with chairing the Board, the Governor is responsible for representing the Central Bank on extrajudicial matters and directing institutional relations with public authorities, financial institutions, and international organizations. Mr. Mario Marcel Cullell was named Governor effective 11 December 2016, for a five-year term[13]/. Mr. Marcel was first appointed to the Board in October 2015.

The Deputy Governor is appointed by the Board, which also specifies the applicable term of office. The Deputy Governor stands in for the Governor when necessary and performs all other tasks entrusted to him. Mr. Sebastián Claro Edwards, who joined the Board as from 7 December 2007 for a ten-year term, was named Acting Deputy Governor as of 21 August 2015. His appointment to the position of Deputy Governor was then renewed in October of that year, effective through the end of his term as Board Member; in the absence of the Deputy Governor, the responsibility of standing in for the Governor, if needed, falls to the longest-standing Member of the Board[14]/.

At year-end 2017, Mr. Claro's replacement as Board Member had not yet been nominated. Consequently, the position of Deputy Governor remained open, so as to allow the election by the full Board.

[12]/ Title II of the Central Bank's Basic Constitutional Act, in accordance with Articles 108 and 109 of the Chilean Constitution, includes the regulations governing the Board and the specific laws applicable to Board Members in terms of their appointment, compensation, incompatibilities, ineligibilities, conflicts of interest, causes for termination of office and other legal obligations inherent to the fulfillment of their duties. The last amendments to that title were Article 7 of Law 20,088 on Equity Affidavit and Law 20,880 on Probity in Public Office and the Prevention of Conflicts of Interest. Additionally, Law 20.730 (on lobbying) entered into force on 29 November 2014 and for all intents and purposes is applicable to the Central Bank of Chile.
[13]/ Through Executive Decree 1404, issued by the Finance Ministry on 26 and published in the *Official Gazette* on 3 December 2016.
[14]/ Board Resolutions 1923E-01-150821 and 1937-01-151029.

The Board of the Central Bank of Chile, 2017.

Effective 29 March 2018, Board Member Joaquín Vial Ruiz-Tagle was appointed the new Deputy Governor, by Resolution 2141-01-180329. He will serve in that position until 28 December 2019, when the next Board Member's term comes to an end[15]/.

The remaining Board Members include Mr. Joaquín Vial Ruiz-Tagle (appointed in February 2012) and Mr. Pablo García Silva (appointed in January 2014), both of whom are serving for a period of ten years from the date of their appointment. Finally, Ms. Rosanna Costa Costa was appointed to replace Mr. Rodrigo Vergara Montes as Board Member, effective 30 January 2017, for the period legally remaining in Mr. Vergara's term, that is, through 28 December 2019[16]/.

On 22 March 2018, Mr. Alberto Naudon Dell'Oro was appointed to fill the position vacated by Mr. Claro, for a term of ten years[17]/.

Generally, the Board is responsible for exercising the authority and fulfilling the tasks entrusted to the Central Bank by law to comply with its mission: to ensure monetary stability and the normal operation of domestic and external payment systems. Therefore, the Board determines the general policies of the Central Bank, issues regulations governing its operation, and supervises the upper levels of the Central Bank. To this end, it also conducts ongoing assessments of compliance with the general rules and policies it has established and the development of institutional activities.

[15]/ Board Resolution 2141-01-180329.
[16]/ Through Executive Decree 29, issued by the Finance Ministry on 23 January 2017.
[17]/ Through Executive Decree 447, issued by the Finance Ministry on 16 March 2018.

Rules governing Board sessions and resolutions

The Central Bank operates essentially through resolutions and agreements passed by the Board in accordance with the organizational statutes governing the Bank.

The Board must hold ordinary sessions at least once a week and special meetings when called by the Governor, either of his own volition or in response to a written request by two or more Board Members. Any resolutions adopted at the meeting must be recorded in the minutes. Board resolutions must be adopted by a quorum of three Members and must have the favorable vote of the majority of those present, except in cases in which the law requires a special quorum for specific resolutions, by reason of their importance or relevance[18]/.

The Board Member chairing the session will cast the deciding vote in case of a tie. The Board generally holds its meetings at its offices in Santiago, but it is empowered to meet and vote on legal resolutions, regulations, or other rulings anywhere within the territory of Chile.

Activities of the Board

In 2017, there were 92 Board meetings and 89 pre-Board sessions. Additionally, during the preparation of each *Monetary Policy Report* and *Financial Stability Report*, the Board held several meetings for coordination, analysis, and discussion.

A.2 Coordination and transparency mechanisms within the institutional structure of the bank

The Central Bank's Basic Constitutional Act establishes the relationships that allow the Bank to adequately fulfill its duties in coordination with the Executive Branch and other government bodies, thereby ensuring suitable control of its actions. Provisions in this area include the following:

(i) Article 6, paragraph 2, of the Basic Constitutional Act, which defines the coordination between the Board and the government, states that on adopting resolutions, the Board shall take into account the general orientation of the government's economic policy.

(ii) Before 30 April of each year, the Bank must submit to the Minister of Finance and the Senate a report on its activities in the previous year, including information on the policies and programs implemented in the period. This *Annual Report* must include the financial statements, with their respective notes and the independent auditors' opinion.

[18]/ A special quorum is required, for example, to approve internal regulations governing Board and Central Bank operations; to override the Finance Minister's veto or suspension of a resolution; to adopt, renew, or suspend foreign exchange restrictions; to receive deposits from the General Treasury or other governmental bodies; and to waive immunity from the enforcement of international contracts entered into by the Central Bank on economic and financial matters.

(iii) With regard to information on the Bank's policies and annual programs, the Basic Constitutional Act further requires that the Central Bank provide a second report to both the Minister of Finance and the Senate no later than 30 September each year.

(iv) It is the Bank's duty to report to the President of Chile and the Senate regarding the general rules and policies it approves in exercising its powers and to advise the Executive Branch, when requested, on all matters associated with the Bank's functions. In this line, Article 1, paragraph 3, of Law 20,789 of 2014, which created the Financial Stability Board, stipulates that this entity will continually consult with the Central Bank on all matters associated with its functions. The Central Bank Governor can participate in all Financial Stability Board meetings and is accorded the right to speak, as well as access to all the information and materials that are analyzed at the meetings, in accordance with the provisions of Article 4 of the Banks's Basic Constitutional Act.

(v) The Minister of Finance can attend Board meetings and is accorded the right to speak and to propose the adoption of certain resolutions. The Minister must therefore be given written advance notice of all calls to Board meetings and the scheduled agenda items.

(vi) The Minister of Finance can suspend any Board agreement or resolution for up to 15 days, unless all Board Members unanimously vote to override the suspension, in which case the suspension will not take effect.

(vii) The Minister of Finance has the right to veto Board resolutions that impose, terminate, or modify foreign exchange restrictions covered under Article 49 of the Basic Constitutional Act, as well as the provision of foreign exchange conventions addressed in Article 47 of that legislation. In the event of a veto, the resolution in question can only be adopted through a unanimous vote by the Board Members.

The last two items aim to promote dialogue with the Executive Branch before the adoption of highly important resolutions, so as to avoid the disruption caused by a suspension or veto. This gives the two bodies the opportunity to overcome differences in opinion with regard to economic measures, although deference is always given to the Bank's autonomy and technical expertise.

In addition to these legal regulations, the Board has established several regulatory provisions aimed at maintaining ongoing communication with the President of Chile, the Senate, and the general public about any measures adopted. This ensures the transparency of its actions and recognizes that the timely dissemination of the Board's decisions plays a crucial role not only in the general public's and the market's perception of the Bank's policies, but also in their impact on the economy.

Consistent with this principle, the Bank continuously incorporates international best practices with the goal of enhancing the transparency of its decisions.

A.3 Board Regulations

The current operating regulations for the Central Bank's Board outline the general rules for Board meetings, including guidelines on notification, the preparation of tables, participation and debate, the preparation of minutes, and the public release of information on the issues discussed, through the respective minutes. They also include special rules on monetary policy meetings, mainly with regard to their frequency, participants, the agenda and debate, minutes, and the dissemination of resolutions through a public press release issued after the meeting.

In November 2017, through Resolution 2110-01-171123, the Central Bank Board introduced significant modifications to its operating regulations with regard to monetary policy meetings.

The changes, which incorporate best practices in monetary policy, include reducing the number of ordinary monetary policy meetings held by the Board to eight meetings in a given calendar year; extending the duration of the meetings to two days; and coordinating the meetings with the preparation of the *Monetary Policy Report*. Additional changes aim to increase the Bank's transparency and the information it publishes. In particular, a more extensive press release on the monetary policy decision will be issued to provide more details on the foundations for the decision and the vote, and the briefings and full record of the monetary policy meetings will be published after ten years, pursuant to the Resolution, in March of each year.

Alejandro Zurbuchen, General Manager of the Central Bank of Chile.

These changes are effective on 1 January 2018, although the annual monetary policy meeting schedule was released in September 2017.

Given the extent and relevance of the changes, the new Board regulations were published in the *Official Gazette*, and the current version is available on the Central Bank's website (www.bcentral.cl).

A.4 General Management, General Counsel, and Auditing

Articles 24, 25, and 26 of the Basic Constitutional Act stipulate that the General Manager is responsible for the direct management and supervision of the Central Bank, in accordance with the instructions and powers granted by the Board. The General Counsel, in turn, has the sole task of safeguarding the Bank's legal structures and monitoring the legal risks associated with the Bank's actions. The Comptroller and Auditor General is responsible for inspecting and auditing the Bank's accounts, operations, and administrative standards.

Mr. Alejandro Zurbuchen Silva has served as General Manager since 7 August 2006. Mr. Juan Pablo Araya Marco has served as General Counsel and Certifying Officer of the Bank since 21 June 2014. Ms. Silvia Quintard Flehan has served as Comptroller and Auditor General since 1 January 2007.

A.5 Audit and Compliance Committee

Through Resolution 1330-01-070419, the Board created the Audit and Compliance Committee and approved the organizational statutes governing it. As an advisory body to the Board, this Committee

reports on the effectiveness of internal control systems and procedures; assesses and reports on the implications for the Bank's equity and reputation of complying with its obligations; assesses the reliability, integrity and timeliness of the information included in the financial statements; coordinates with the Bank's Comptroller and Auditor General in terms of the responsibilities assigned by the Basic Constitutional Act; and proposes the hiring of independent auditors.

In 2017, the Committee met eight times. The issues addressed at these meetings included assessing the services provided by the independent auditing firm; reviewing the annual auditing plan and final report; being briefed on the annual internal auditing plan and its execution; and reviewing the Bank's risk management, internal monitoring, and information systems.

The Committee is chaired by Mr. José Luis Cea Egaña, who was appointed to this position on 16 June 2014. In 2017, the other members of the Committee were Mr. Gustavo Favre Domínguez and Mr. Jesús Riveros Gutiérrez. The latter was replaced on 22 August 2017 by Mr. Anthony Dawes Martindale, as per Board Resolution 2085E-01-170822.

B. Internal Management

B.1 Strategic Planning

Strategic Plan 2018-2022

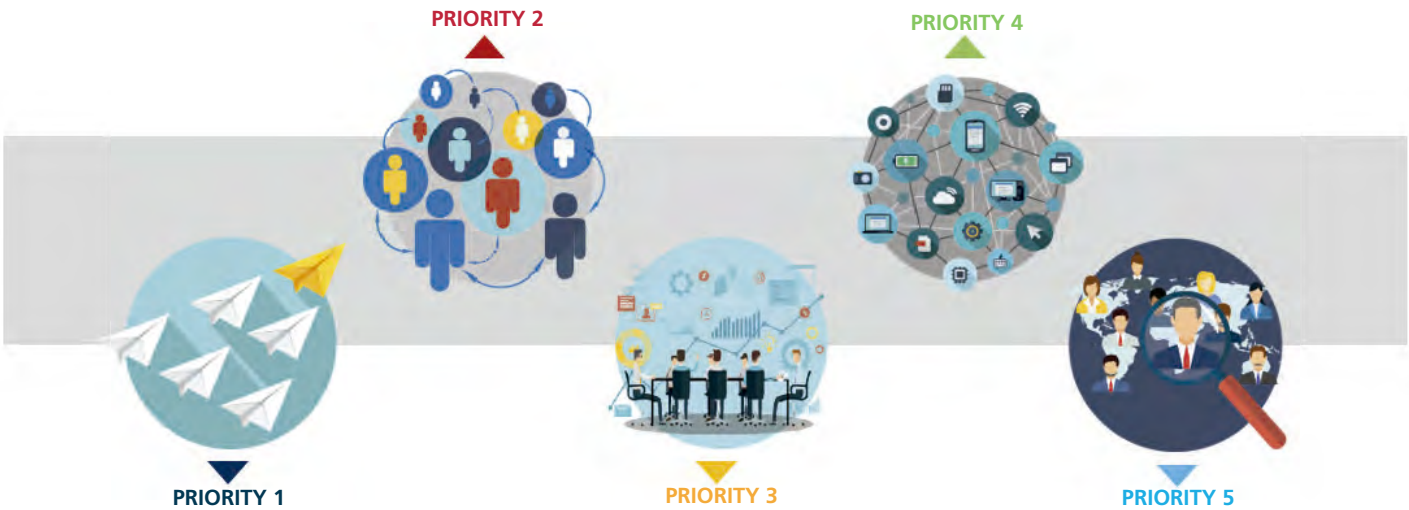
The Central Bank of Chile's vision is to be a trustworthy technical institution, known for its high standards in achieving its institutional objectives.

Its mission is to safeguard the stability of the currency and the normal operation of the internal and external payment systems, thereby contributing to the smooth functioning of the economy, financial stability, and the well-being of the community.

The Bank's strategic planning plays an important role in the achievement of its vision and mission in changing contexts and the ability to respond to the new economic, financial, legal, technological, and social demands that are emerging at the national and international levels. Since 2004, these exercises are conducted for a horizon of five years, coinciding with the term of office of the Bank's Governor.

In 2017, the strategic plan for the 2018–2022 period was developed through a consultative, participatory, and inclusive process, envisioned as "A Project for All". This theme captures the fact that the Bank is not an isolated entity, but rather works for the country as a whole and depends fundamentally on the people who make up the organization. Consequently, the groundwork for developing the 2018-2022 Strategic Plan included over 100 internal and external interviews, a broad opinion poll, surveys of regional and international focus groups, internal staff workshops, planning workshops with active participation of the Central Bank's Board, Division Directors, and managers, and ongoing communication on the progress and results of the process.

STRATEGIC PRIORITIES



This process led to the identification of five strategic priorities, which will provide the foundation for the corporate agenda over the next five years. These priorities are as follows:

- Strengthening the Bank's response capability and intellectual leadership in order to achieve the institutional objectives defined in the Basic Constitutional Act, incorporating an increasingly complex reality.

- Strengthening the Bank's understanding of and dialogue with its wider environment through strategic communications management that identifies objectives, roles, and functions.

- Strengthening the Bank's corporate governance so as to balance risk tolerance and business process efficiency, streamlining the decisionmaking process and facilitating innovation.

- Improving the Bank's capacity to understand, manage, and incorporate technological changes, in relation to both its operations and management and its institutional objectives.

- Being an employer of excellence, offering a value proposition that inspires people and teams to discover and develop their full potential, in a work environment that promotes collaboration, continuous learning, and professional and personal challenges; and thus attracting and retaining talent, in line with the Bank's strategic objectives and corporate values.

The implementation of the initiatives and lines of action associated with each of these five priorities will allow the Bank to successfully face the challenges of a fast-changing environment over the coming years, including a society that demands more from its institutions in terms of transparency, probity, excellence, and trust.

This plan represents a commitment on the part of the entire staff of the Central Bank of Chile, to enrich our primary asset as a public institution: trust. Trust, more than laws and standards, is precisely what sustains the legitimacy and autonomy of our institution.

Strategic Plan 2013-2017

This year, 2017, was the fifth and final year of the 2013-2017 Medium-Term Strategic Plan. The strategic priorities during this period were the following:

- Strengthening the financial stability objective.
- Aligning people, services, and resources with the Bank's primary focus.
- Renovating and optimizing treasury processes.
- Consolidating the Bank's internal governance and institutional structures.

Based on these strategic definitions approved by the Board, the different units worked on their strategic projects and initiatives and submitted a budget request for their implementation, prioritizing areas aligned with the above focal points so as to achieve the Bank's objectives. The rest of this section describes the most important achievements for each strategic priority.

Strengthening the financial stability objective

In this area, the main achievements were the following:

a. Strengthening of the *Financial Stability Report*, which was recognized in 2017 by the International Monetary Fund as one of the best in the region.

b. Strengthening of statistics for financial analysis, in particular with regard to the generation and communication of the Household Financial Survey.

c. Strengthening of applied research and analysis on issues related to financial stability.

d. Analysis, implementation, and collaboration on the application of regulatory changes, with modifications to the *Compendium of Financial Regulations* and the *Compendium of Foreign Exchange Regulations*.

e. Publication of the new national accounts series, based on the 2013 Benchmark Compilation.

Aligning people, services, and resources with the Bank's primary focus

In this area, the main achievements were the following:

a. Creation of the Ethics Committee and launch of an internal complaints channel.

b. Launch of a new employment evaluation tool.

Renovating and optimizing treasury processes

In this area, the main achievements were the following:

a. Elimination of the $1 and $5 coins, application of the rounding rule, and development of a publicity campaign, which had wide media coverage.

Consolidating the Bank's internal governance and institutional structures

In this area, the main achievements were the following:

a. Implementation of operational risk and performance measures for interest rate futures.

b. Launch of an Educational Space at the Central Bank, together with a board game, *EconómicaMente*, that fosters learning and awareness of economic concepts.

c. Certifications: ISO 27001 on Information Security, including confidential and highly sensitive information (HSI); ISO 22301 on Business Continuity, including the payments system and the processes of the Security, Logistical Services, Institutional Affairs, and Information Systems Managements of the Bank; International Certification for the Professional Practice of Internal Auditing in the Central Bank of Chile, by the Board of Governors of the U.S. Federal Reserve System; ISO 9001:2015 Certification on Purchasing Procedures; maintenance of certification of internal auditing processes under the International Standards for the Professional Practice of Internal Auditing; recertification of quality assurance, accounting, security, and service processes under ISO 9001:2015 standards.

d. Completion of the recovery and restoration of the north and west faces of the Central Bank building.

B.2 Organizational Structure, Internal Restructuring, and appointments

In April, through Resolution 2034E-01-170125, Ms. Solange Berstein Jáuregui was named Director of the Financial Policy Division. She replaced Mr. Claudio Raddatz Kieffer.

In July, through Resolution 2066-01-170525, Mr. Juan Carlos Piantini Cardoso was appointed Manager of International Markets, replacing Mr. Ricardo Consiglio Fonk.

In September, through Resolution 2088E-01-170831, Ms. Marcela Pumarino Cruzat replaced Ms. María Angélica Arteaga Arriagada as Manager of Human Resources.

In January, Ms. María de los Ángeles Arias was appointed Head of the Talent Management and Organization Department, replacing Mr. Sebastián Aguirre Gran.

In May, Ms. Patricia Medrano Vera was appointed Head the Microdata Department.

In July, Mr. Oscar Giusti Bueno was named Head of the International Desk Department, replacing Mr. Juan Carlos Piantini Cardoso; and Mr. Mauro Villalón Sepúlveda was appointed Head of the Investment Strategy Department.

B.3 Human resources Management

A new selection process was implemented in 2017, which includes the application of an online cognitive ability test as a first filter and a skills-based assessment, based on a behavioral event interview, at the end of the process. Additionally, the average length of the hiring process decreased compared with last year, from 86 to 67 days.

Succession plans were completed for all high positions, with a total of 86 positions reviewed.

In September 2017, the fourth Organizational Climate Survey was implemented, using the same tool as previously; the results were returned in November. The Bank saw a significant improvement of 4 percentage points relative to the 2016 survey. This improvement reflects organization-wide efforts, work in individual departments to address specific priorities and actions for improvement, and strong support from the Board and upper management. In addition, a new approach was defined for supporting the units with the lowest climate results, with the provision of complementary external consulting to assist with qualitative diagnostic assessments and the definition of improvement actions.

Performance management processes were adjusted to include the elaboration of skill-development plans for all Bank employees, in order to identify, design, and plan training actions that foster the development of technical and behavioral skills, with a focus on strengthening employees' performance in their current positions and/or preparing them to face new challenges within the Bank.

A leadership skills development program was implemented over the course of the year, with workshops on feedback, effective hiring interviews, difficult conversations, organization and planning, and the elaboration of skill-development plans. There was a high degree of participation in the workshops: 81% of heads of departments attended at least one workshop (108 out of 133). As a result of these workshops, together with ongoing mentoring and occasional coaching support for specific cases, the 2017 climate survey saw an increase of 11 percentage points on questions related to direct heads, relative to 2016. Other training efforts in 2017 included the continuation of the English program, with 103 employees participating in classes over the course of the year.

The Bank awarded seven scholarships for international graduate studies, of which five were for master's degree programs and two for Ph.D. programs. Nationally, five scholarships were awarded for master's degree candidates and seven for undergraduate degree programs.

In 2017, there were 210 training activities, equivalent to 19,113 training hours, which reached a total of 526 staff members, thus averaging 30.3 hours per person. The budget execution related to training activities in 2017 was around 94% use.

B.4 Office of the Comptroller and Auditor General

The Office of the Comptroller and Auditor General is focused on helping the Board, the Audit and Compliance Committee, and Management fulfill their duties, through an independent, objective, and systematic evaluation of the design and effectiveness of risk management, internal control, and management systems. The Office also provides consulting services that add value and support the achievement of institutional objectives.

In 2017, the Bank maintained its quality assurance certification by the Institute of Internal Auditors, reaffirming that the Central Bank's auditing activities "comply with international standards for the professional practice of internal auditing." The Bank also maintained certification of its process, "Internal Auditing Services for the Central Bank of Chile," under ISO 9001:2015 standards.

B.5 Main administrative contracts for the provision of goods and services

The Bank is subject to the provisions in its Basic Constitutional Act governing the periodic release of information on the fulfillment of its public duties. In this context, this report discloses the main contracts signed by the Bank in 2017 for an amount over Ch$100 million, which are related to the supply of goods and services that allow the institution to operate normally (table 2.1) and annual expenditures on consultant services, surveys, research, and seminars (table 2.2).

TABLE 2.1

ADMINISTRATIVE CONTRACTS SIGNED IN 2017, FOR OVER CH$100 MILLION

N°	Supplier	Note	Purpose	Effective	Ending
3506	Sistemas Integrados de Computación y Telecomunicaciones S.p.A.		Infrastructure maintenance services	15-Jun-2017	28-Feb-2018
3511	FireEye, Inc.		Information and technology services	07-Jun-2017	07-Jun-2018
3585	Hitachi Data Systems Chile Ltda.		Information and technology services	28-Sep-2017	28-Feb-2018
3600	Orange Business Services Chile S.A.		Information and technology services	14-Dec-2017	10-May-2018
3644	Paisajismo Hermano Arbol S.A.	(*)	Infrastructure maintenance services	01-Dec-2017	01-Dec-2018

(*) One-year contract, which is automatically renewable for up to four additional one-year periods.

TABLE 2.2

EXPENDITURES ON CONSULTING, SURVEYS, RESEARCH, AND SEMINARS (1)

(2017 Ch$ million)

	2013	2014	2015	2016	2017
Consulting, surveys, research, and seminars	1,717.7	2,552.6	2,190.1	2,582.7	2,254.7
Consulting (2)	1,019.8	1,014.3	1,127.1	1,664.2	1,156.3
Surveys and research (3)	421.1	1,123.5	616.7	600.8	755.4
Seminars	276.8	414.8	446.3	317.7	343.0

(1) The average CPI was used to update older figures to 2017 pesos (base year 2013).
(2) The increase in 2016 relative to earlier years is largely explained by consulting services associated with the cash center project.
(3) The increase in 2014 relative to earlier years is largely explained by the household financial survey and the 2013 benchmark compilation. The latter is carried out every five years.

Source: Central Bank of Chile.

Section E.3 provides general information on the contracts signed by the Bank in connection with the 2017 issue program.

C. PERSONNEL, ADMINISTRATIVE, AND OTHER EXPENSES

These management-related expenses include personnel compensation and benefits; the use and consumption of goods and services; and other expenses necessary for carrying out the Bank's activities (table 2.3). On the income statement, they are broken down as follows: (i) personnel and administrative expenses; and (ii) other expenses and income. In 2017, of the total personnel, administrative, and other expenses, personnel costs represent 63.9%; administrative expenses, 32.7%; and retirement benefits, 3.4%.

Personnel expenses

Personnel expenditures were stable in real terms between 2016 and 2017. In the year, the total staff increased to 666 people (645 in 2016). Professionals accounted for 77.3% of the total staff as of December 2017.

TABLE 2.3

PERSONNEL, ADMINISTRATIVE, AND OTHER EXPENSES (1)

(2017 Ch$ million)

	2013	2014	2015	2016	2017
Personnel and administrative expenses					
Personnel expenses	32,326.8	32,986.1	35,548.9	36,370.8	36,353.3
Administrative expenses	16,736.5	17,403.5	19,082.2	19,029.3	18,588.2
Provision for post-employment benefits	1,656.4	1,419.2	1,494.8	1,898.9	1,908.2
Total	**50,719.7**	**51,808.8**	**56,125.9**	**57,299.0**	**56,849.7**
Other expenses and (income)					
Depreciation, amortization	3,224.8	3,184.7	2,811.1	3,508.9	2,754.0
Taxes and contributions	633.0	651.2	762.8	636.7	639.8
Other	99.4	(14.9)	(62.2)	(1.0)	395.8
Total	3,957.2	3,821.0	3,511.7	4,144.6	3,789.6
Subtotal personnel, administrative, and other expenses	**54,676.9**	**55,629.8**	**59,637.6**	**61,443.6**	**60,639.3**
Sinap liquidation impairment, Law 18,900 (2) and (3)	0.0	1,147,138.7	(79,697.1)	0.0	0.0
Total personnel, administrative, and other expenses	**54,676.9**	**1,202,768.5**	**(20,059.5)**	**61,443.6**	**60,639.3**
A. Personnel expenses					
Wages and other employer contributions	27,759.6	28,287.2	30,808.9	31,502.1	32,053.7
Employee well-being	3,592.1	3,780.4	3,797.1	3,962.8	3,433.1
Training	975.1	918.5	942.9	905.9	866.5
Total	**32,326.8**	**32,986.1**	**35,548.9**	**36,370.8**	**36,353.3**
B. Administrative expenses					
Utilities	1,091.5	1,030.4	1,261.0	1,229.9	1,220.7
General services	5,383.7	5,944.7	6,806.0	6,420.5	6,862.7
Maintenance of fixed assets	2,803.3	2,310.4	2,278.0	2,113.3	2,590.5
Computer and technological development expenses	5,740.3	5,565.4	6,547.1	6,682.9	5,659.6
Consulting, surveys, research, and seminars	1,717.7	2,552.6	2,190.1	2,582.7	2,254.7
Total	**16,736.5**	**17,403.5**	**19,082.2**	**19,029.3**	**18,588.2**

(1) The average CPI was used to update older figures to 2017 pesos (base year 2013).
(2) Due to the recognition of a provision for impairment of the total value of the credit recorded on the balance sheet stemming from the entities that made up the National Savings and Loan System (Sinap).
(3) The net income in 2015 basically corresponds to the recovery of the impairment of the Sinap liquidation asset (Law 18,900) recorded the previous year, in accordance with IFRS.

Source: Central Bank of Chile.

Administrative expenses

Administrative costs recorded a real decrease of 2.3% between 2016 and 2017. This was mainly due to a reduction in expenditures on computers and technological development and on consulting, surveys, research, and seminars; which was partially offset by an increase in maintenance of fixed assets and general services.

D. COMMUNICATION AND DIFFUSION

D.1 Main Publications

The main objectives of the Central Bank's publication program are to increase the transparency of its communication, improve the quality and timeliness of its delivery of economic information, and provide the public with information on key economic issues.

The main publications through which the Bank communicates its policies are the *Monetary Policy Report* and the *Financial Stability Report*. The former, which is published quarterly in March, June, September, and December, presents the Board's assessment of the recent and expected evolution of inflation, its implications for monetary policy, the medium-term analytical framework used in monetary policy formulation, and the information necessary for agents to adequately formulate their inflation and economic growth estimates.

The *Financial Stability Report*, which is published half-yearly (in June and December), reports on recent macroeconomic and financial developments that could affect the financial stability of the Chilean economy. The report also presents the policies and measures that support the normal functioning of the internal and external payment systems, with the goal of promoting public knowledge and debate on the Bank's actions in carrying out its functions.

In 2017, in conjunction with the September *Monetary Policy Report*, the Bank published a report on *Trend Growth: Medium-Term Forecast and Analysis of the Determinants*. This in-depth discussion of medium-term trend growth in Chile, over the 2017–2050 horizon, focused in particular on the forecast for non-natural-resource and total GDP over the next ten years.

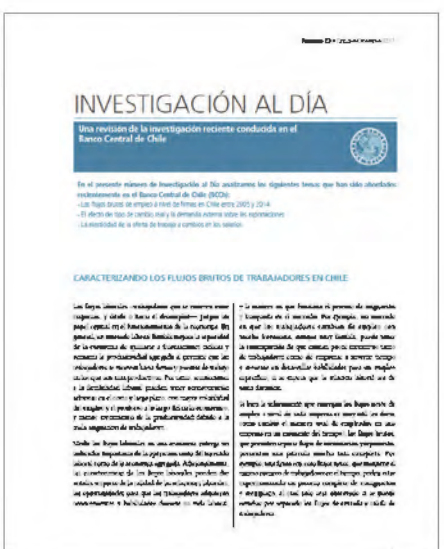
The Bank continued to publish the *Business Perceptions Report* (BPR). This quarterly report—published in February, May, August, and November—summarizes the opinions and perceptions of corporate executives from approximately 220 firms from across the country. The interviews are carried out by economists from the Monetary Policy Strategy and Communication Management.

The Bank's work in economic research is also reflected in the nine papers and six research notes published in the journal *Economía Chilena*. This publication, which is published three times a year (in April, August, and December), addresses issues affecting the Chilean economy, with a strong empirical focus and an emphasis on issues relevant for the conduct of economic policy.

Monetary Policy Report.

Financial Stability Report.

Journal: *Economía Chilena.*



Document: *Current Research.*

In 2017, four new papers were published in the *Economic Policy Papers series*. This series discloses the thinking of Central Bank authorities on issues relevant to the economy and the conduct of monetary policy. The topics analyzed this year were financial monitoring and the communication of financial stability issues from the perspective of the Chilean experience; the economic constitutionalism and institutional autonomy of the Central Bank; technological innovation and evolution in financial services (FinTech) and what it implies for the banking industry; and the challenges of systematic monetary policy.

The Bank also published 16 *Working Papers* in 2017. This series has been positioned as a leading economics publication at the international level, based on the number of Internet hits. Its purpose is primarily to facilitate the exchange of ideas and to release preliminary economic research results for discussion and commentary.

The publication *Investigación al Día* (Current Research) is another outlet for research papers generated by the Bank. Its main objective is to summarize the current research underway at the Central Bank of Chile. This quarterly series issued four new papers in 2017.

Six new papers were published in the *Research in Economic Statistics series* this year. The purpose of this series is mainly to release research papers on economic statistics, with a strong empirical content. The papers addressed the following topics: the evolution of market risk regulations in the Chilean banking sector; a measure of capital services for the Chilean economy; the characterization of the debt of non-bank firms in Chile; the characterization of mortgage interest rates; historical GDP and expenditure the 1986-2013 period; and the Central Bank's balance sheet from 1926 to 2015.

Finally, in accordance with the provisions of Article 53 of its Basic Constitutional Act, the Bank continued its annual program of recurrent publications, aimed at disseminating information on the main national macroeconomic statistics. This year's publications included the following: *Informativo Diario de Operaciones Financieras Nacionales* (Daily Bulletin on National Financial Operations); *Informe Mensual de Estadísticas Monetarias y Financieras* (Monthly Monetary and Financial Statistics Report); *Informe Mensual de Estadísticas del Mercado Cambiario* (Monthly Foreign Exchange Market Statistics Report); *Serie de Datos Bancarios* (Bank Data Series); *Boletín Mensual* (Monthly Bulletin); *Indicadores de Comercio Exterior* (Foreign Trade Indicators); *Indicadores Macroeconomics y de Coyuntura* (Macroeconomic and Current Indicators). In addition, digital yearbooks and quarterly reports were published on Chile's balance of payments, international investment position, external debt, national accounts, national accounts by institutional sector, and statistical synthesis.

D.2 Visits to the Senate and the House of Representatives

The Board presented the *Monetary Policy Report* to the Senate Finance Committee in Santiago on 3 April, 5 June, and 4 December and to the full Senate in Valparaíso on 6 September. The June and December presentations included the *Financial Stability Report.*

The Board speaks before the full Senate in Valparaíso.

Presentation of the *Monetary Policy Report* and the *Financial Stability Report.*

Monetary Policy Meeting.

The Central Bank Deputy Governor, Sebastián Claro, gave a presentation to the Senate Economics Committee on 11 October in Valparaíso, on the bill to modify Law 20,009, limiting the responsibility of the users of credit/debit cards and other means of payment in the case of fraud (Boletín N° 11.078-03).

In the House of Representatives, Governor Mario Marcel spoke before the Finance Committee in Valparaíso on two occasions: on 7 March, to discuss the bill creating a new institutional structure for the national statistics system; and on 20 June, to discuss the General Banking Law reform bill. In addition, on 21 August, he addressed the House Labor and Social Security Commission in Santiago, on the bill to create the new collective savings system, increase the coverage of the pensions system, and strengthen the solidarity pillar.

D.3 Seminars, Workshops, and Conferences

Within the program of seminars, conferences, and workshops organized by Central Bank in 2017, the Financial Regulation and Infrastructure Management of the Monetary Policy Division organized a seminar on Financial Market Infrastructures: Developments and Challenges on 9 January, which analyzed the results of a recent market infrastructure assessment carried out by the World Bank and the IMF, called the Report on the Observance of Standards and Codes (ROSC). Speakers included representatives of the Deutsche Bundesbank, the Central Bank of Brazil, the Federal Reserve Bank of New York, and the World Bank, as well as authorities and representatives of the national financial infrastructure.

On 15–18 May, the first Regional Workshop on the Instrumentation of Central Bank Operations was organized by the Central Bank's Payment Systems and Operations Management, in conjunction with the Latin American Center for Monetary Studies (Cemla) and the Deustche Bundesbank. The meeting was attended by representatives of the European Central Bank and 12 countries: Barbados, Colombia, Costa Rica, Curaçao, Chile, Guatemala, Honduras, Jamaica, Mexico, Paraguay, Dominican Republic, and Surinam. The objective was to promote the exchange of ideas and knowledge in order to improve understanding of the operational framework of central banks' monetary policy, as well as the techniques and procedures for its instrumentation.

On 30 May, the Financial Regulation and Infrastructure Management organized the twelfth meeting of the Regional Consultative Group for the Americas of the Financial Stability Board (FSB), whose function is to monitor the global system and make recommendations as needed. The event was attended by the Governor of the Central Bank of Chile, Mario Marcel; other national authorities; and the Senior Deputy Governor of the Bank of Canada, Carolyn Wilkins, who was the principal moderator during the day. The panel discussions featured the Governor of the Central Bank of the Bahamas, John Rolle; the Secretary of the Central Bank of Barbados, Sadie Dixon; the Senior Vice-President of the Resolution Division of the Canada Deposit Insurance Corporation (CDIC), Michael Mercer; the Chief of Staff of the Deputy Governor of the Central Bank de Brazil, João Andre Pereira; and the Senior Deputy Secretary of Legal Affairs of the Mexican deposit insurance agency (IPAB), Mario Luna. The Director of the Financial Markets Department of the Bank of Canada, Harri Vikstedt, and the Senior Deputy Director, Supervisory Examinations, of the de Division of Risk Management Supervision of the U.S. Federal Deposit Insurance Corporation, James C. Watkins, participated via remote connection.

On 24–26 May, the Economic Research Management organized a course on Aggregate Productivity, Imperfect Allocation, and Firm-Level Data, taught by Professor Virgiliu Midrigan from New York

University. Professor Midrigan studied economics at the American University in Bulgaria and holds master's and doctorate degrees from Ohio State University in the United States.

On 3 August, the Economic Research Management organized a seminar on the Macroeconomics of Granularity and Production Networks, which reviewed work on the macroeconomic implications of input-output ratios, in particular, aggregate productivity, economic cycles, and monetary policy. The speakers included Xavier Gabaix (Harvard University), Ezra Oberfield (Princeton University), Michael Weber (University of Chicago), and David Baqaee (London School of Economics). The discussants were Gustavo Ventura (Arizona State University), Bernard Herskovic (University of California at Los Angeles), and Carlos Carvalho (Central Bank of Brazil).

On 4–6 September, the Economic Research Management organized a course entitled "Introduction to the Econometrics of High-Dimensional Models." The course was taught in three modules by Professor Christian Hansen from the Booth School of Business at the University of Chicago.

On 7–8 September, the VII Financial Stability Meeting was held in Viña del Mar, organized jointly by Cemla and the Central Bank. The event brought together authorities responsible for financial system regulation, supervision, and monitoring in central banks, financial supervisory agencies, and multilateral organizations in the region, who analyzed the financial-economic situation of Latin America, economic risk, prospective risks for nonbank entities, the real estate sector, and external financing, as well as issues related to stress testing in banks and nonfinancial companies. The speakers included Fabrizio Zampolli, from the Bank for International Settlements (BIS); Kataro Ishi and Jorge Chan-Lau, both from the IMF; and Oscar Carvallo, from Cemla.

On 3–4 October, the Statistics Division organized the II Conference on Statistics: Measuring the Economy in a Globalized World, which was attended by representatives from 23 countries, including Argentina, Germany, Aruba, Bolivia, Brazil, Canada, Colombia, Dominican Republic, France, Guatemala, Guyana, Honduras, Mexico, Paraguay, Peru, Portugal, Spain, Surinam, United Kingdom, United States, and Uruguay. Before an audience of 240 guests, the panelists presented the experience of different international organizations, central banks, and national statistics offices and discussed the opportunities that are emerging in a new dynamic, digital, interconnected economy. The speakers included Sandra Cannon, Federal Reserve Bank of Kansas; Sanjiv Mahajan, U.K. Office for National Statistics; Jens Mehrhoff, Bundesbank; Laurence Allain, IMF; Paul Schreyer, OECD Statistics Directorate; and Aurel Schubert, European Central Bank Statistics Department.

On 4–5 October, the Bank hosted the third Forum of Financial Information of Latin American and Caribbean Central Banks, organized jointly with Cemla. The topics covered at the meeting included the experience of central banks in Europe, in particular in Spain and Portugal, on repositories for corporate financial statements used in the analysis of financial stability; a review of the exchange of information among financial regulators in the cases of Colombia, Mexico, the United Kingdom and the recommendations of the Bank for International Settlements (BIS) in this area; and the importance of financial inclusion in the light of the experience in Argentina, Chile, Paraguay, and Spain. The latter session was moderated by the Chilean Superintendent of Banks and Financial Institutions, Eric Parrado.

XXI Annual Conference on "Monetary Policy and Financial Stability: Transmission Mechanisms and Policy Implications

On 16 October, Claudio Raddatz, the Division Chief of the IMF Global Financial Stability Analysis Division, presented the Global Financial Stability Report (GFSR), accompanied by the Director of the Central Bank's Financial Policy Division, Solange Berstein. The presentation included an analysis of the challenges facing financial systems.

On 16–17 November, the Central Bank held its XXI Annual Conference, on Monetary Policy and Financial Stability: Transmission Mechanisms and Policy Implications. The program was arranged by Markus Brunnermier, a researcher at Princeton University, and staff members of the Central Bank of Chile. The conference was divided into five sessions: Monetary Policy Channels and Financial Stability; Capital Flows, Macroprudential Policy, and Capital Controls; Financial Stability in Emerging Economies; Implications for Monetary and Macroprudential Policy Conduct and Design; and Monetary Policy. The meeting was attended by leading economists from the European Central Bank, the IMF, and the BIS; research centers such as the Stanford School of Business, Paris Institute of Political Studies, Rutgers University, Stockholm School of Economics, the University of Southern California, and the Stern School of Business at the New York University; and the central banks of Brazil, India, and Thailand. The conference ended with a presentation by Sir Paul Tucker, Chair of the Systemic Risk Council and Senior Fellow at the Harvard Kennedy School and Harvard Business School. Videos of the main presentations are available on the Central Bank of Chile's YouTube channel.

On 22 November, the Statistics Division organized a workshop on Economic Tendency Surveys. The workshop discussed current best practices on business and consumer perception surveys as outlined in the United Nations Handbook on Economic Tendency Surveys; reviewed the experience of the European Commission and the Bank of Canada, demonstrating the utility for economic authorities and researchers of the survey data on output and the economic cycle and their use in forecasting; and explored technical aspects of survey design, data collection methods, and the diffusion of results.

On 7 December the Economic Research Management of the Research Division held a workshop on Beliefs, Sentiments, Confidence, and the Macroeconomy, with a keynote speech by Professor George-Marios Angeletos from the Massachusetts Institute of Technology (MIT). The first panel discussion, entitled Sentiments, Confidence, and Its Macroeconomic Impact, featured Nitya Pandalai Nayar, University of Texas-Austin; Andrei Levchenko, University of Michigan; George Evans, University of Oregon; Seppo Honkapohja, Bank of Finland; and Kaushik Mitra, University of Birmingham. The second panel, Sentiments, Confidence, and News: Empirical Relevance, featured Mark Spiegel, Federal Reserve Bank of San Francisco; Jess Benhabib, New York University; Patrick Fève, Toulouse School of Economics; Alain Guay, University of Quebec—Montreal (UQAM); Olivier Coibion, University of Texas-Austin; Yuriy Gorodnichenko, University of California–Berkeley; and Saten Kumar, Auckland University of Technology.

D.4 Community Outreach Program

Over the course of the year, the Bank strengthened its community outreach program, Central to Your Life, maintaining an active relationship with the public via two lines of work: economic and financial education and media relations. A variety of actions and tools were employed to disseminate information on the Bank's role in the economy and in people's daily lives. As part of this role, the Bank participated as a permanent advisor to the Advisory Commission for Financial Inclusion, led by the Finance Ministry, which submitted the National Financial Education Strategy to the President of Chile in early January 2018.

The numismatic museum has become an important point of interest for the public. Over the course of the year, more than 4,900 people participated in scheduled tours, nearly 2,000 came as walk-ins, and 2,050 visited on National Heritage Day.

The ninth training seminar for journalists was held between June and November 2017. The program is organized annually by the Bank in conjunction with the Chilean Chapter of the Inter-American Association of Economic and Financial Journalists (AIPEF). The objective of the seminar is to contribute to the professional development of journalists interested in expanding or deepening their knowledge on economic issues related to the Bank's work. As in past years, the eight workshops in the series were led by the Central Bank Governor, one of the Board Members, Department heads, and one of the Bank's senior economist, who discussed a range of topics including monetary policy, financial regulation, and statistics. The talks were attended by 54 journalists from different communications areas, including news agencies, broadcasters, public organizations, and businesses, as well as private journalists.

With regard to social networks, the Bank has had an official Twitter account (@bcentralchile) since April 2013, which had over 17,000 followers as of 31 December 2017; a YouTube channel (www.youtube.com/user/BancoCentralChile) since May 2014, with 147 videos and over 1,300 subscribers at year-end; and a Flickr account (www.flickr.com/photos/bancocentraldechile) since July 2016, with around 87,000 visits as of December.

Seminar for journalists, organized in conjunction with the Inter-American Association of Economic and Financial Journalists (AIPEF) .

This was the eleventh year that the Bank presented its training workshops, Know Your Banknotes, a diffusion program on the banknotes in circulation and their security features. The program is a key element for maintaining and strengthening the integrity of this payment means and reinforcing the trust not only of people who work with cash in their work, but also the public at large.

In 2017, a total of 2,231 people received training, mainly cashiers from retail establishments, small businesses, and commercial banks, as well as student cashiers in training at technical institutes and the general public. Most of the workshops were held in Santiago this year, although activities were also organized in counties such as Melipilla, Valdivia, Osorno, and Arica.

To support the Know Your Banknotes initiative and to satisfy the needs of businesses and other organizations, 26,277 informational products (brochures, pamphlets, posters, and stickers) were distributed to provide information on the security features that facilitate the recognition of authentic bills, as well as banknote identification devices for the visually impaired.

Website www.billetesymonedas.cl

As part of this training initiative, the Bank continued its Training for Trainers Program, which has greatly expanded the scope of diffusion on banknote security features. This program allows businesses and institutions to train their own staff to give workshops to company employees, students, and vulnerable members of the community, using materials provided by the Bank. The initiative, which was launched in 2014, had agreements with 39 businesses as of December 2017.

In June 2017, the bank launched a new educational website, www.billetesymonedas.cl, which provides complete information on the history, recognition features, security measures, and recommendations for use of the Chilean bills and coins. The aim is to give people information on the currency, in an easy-to-use and attractive format, including information on the current regulations on counterfeit and damaged banknotes and how to exchange worn or damaged bills at the Central Bank or at commercial banks throughout Chile. The site is accessible for the visually impaired and can be used on different devices, including smartphones and tablets.

The Bank also continued its training program for the national police institutions (*Carabineros de Chile and Policía de Investigaciones de Chile*), which was launched in 2013 with the objective of facilitating police interaction with citizens regarding the recognition of legal banknotes. In 2017, there were 39 national workshops and three seminars for forensic experts, reaching a total of 3,072 officers.

In conjunction with the Investigative Police, the Bank implemented an informational campaign on the banknote security features in the month of July, oriented mainly toward tourists who arrive in the country via the Arturo Merino Benítez International Airport in Santiago.

A similar initiative was coordinated with *Carabineros de Chile* during the Independence Day holidays in September, with officers visiting shopping areas in Santiago to talk with shop owners and customers in order to explain the banknote security features, demonstrate how to verify the authenticity of banknotes, and hand out print materials. *Carabineros de Chile* then replicated the campaign at the national level.

In 2016 the Bank continued to implement its statistical diffusion program, aimed at promoting the use and understanding of the statistics the Bank generates. This year, the program focused on holding one-day workshops in Concepción and Puerto Montt. The presentations reviewed the main concepts, methodology, and results of the balance of payments, national and regional accounts, and foreign exchange market statistics.

As in previous years, teacher training workshops were organized to provide instructional tools for teaching students about the Bank's functions. Four workshops were held at the Bank in January and July, with the attendance of 50 teachers from around the country. An additional workshop was held in Valdivia in November, in conjunction with the Education Quality Agency; nearly 50 teachers attended.

New teaching resources were released in 2017 to support the Bank's work in economic and financial education. These include the Educational Space in the main hall of the Central Bank building, which is set up to receive school field trips in a classroom-like atmosphere, with a modular design around a series of panels that present economic concepts and information on the main functions of the Central Bank. The space supports interactive learning and features one of the year's other educational innovations: namely, a board game, EconomicaMente, which provides a fun and dynamic way for students to learn about the Bank's role in the country's economy and issues related to financial decisionmaking on saving, credit, and investment.

Another innovation was the launch of a new animated video series, EconoAmigos, centered on a group of children who experience a variety of day-to-day situations, which provide an entertaining platform for learning about the Bank's functions, the meaning of inflation, the importance of the monetary policy rate, the implications of debt, the concept of money, and the functioning of foreign trade.

The guided tour program for schools was redesigned in 2017, to incorporate a more educational focus. The new educational tours, which started in August, are aimed mainly at students from eighth grade through senior year of high school. The new tour includes a workshop for learning concepts related to the Bank's main functions. Students visit the numismatic museum to cover material brought by the students, followed by a round of the board game, EconomicaMente, in the Educational Space. Nearly 3,600 students and teachers participated in school tours in 2017.

Educational Space in the main hall of the Central Bank building, which is set up to receive school field trips in a classroom-like atmosphere.

EconomicaMente, a board game that provides a fun and dynamic way to learn about the Bank's role in the country's economy.

EconoAmigos, an animated video series centered on a group of children who experience a variety of day-to-day situations, through which they learn about the Bank's functions.

In addition to high school students and teachers, 986 Chilean and foreign university students visited the Bank, where they saw a presentation on the role and functions of the Central Bank.

For the fourth consecutive year, the Bank took part in Global Money Week, an event promoted by the Dutch NGO Child and Youth Finance International. The event included a Twitter rally in which students throughout Latin America answered questions from participating organizations. In the case of the Central Bank, the question was "What tool does the Bank use to monitor price stability?" The Chilean winner was Karina Sureda from the county of *Ñuñoa*.

The Bank participated in the fourth annual Financial Education Fair, held on 4–5 October at the *Palacio La Moneda* Cultural Center and organized by the SBIF. The Fair was opened by the President of Chile, Michelle Bachelet, who was accompanied by Governor Mario Marcel. The Bank had a stand with educational material and the new board game, EconomicaMente. There was also a character portraying the $10,000 bill, who interacted with visitors and encouraged them to participate in a trivia contest with questions related to the Bank's functions. Some of the new videos in the EconoAmigos animation series were also shown.

In its role as a permanent advisor to the Advisory Commission on Financial Inclusion, the Bank worked actively on the formulation of a National Financial Education Strategy. Once approved, the final draft was submitted to the President of Chile by the Commission, led by the Finance Ministry and including several public sector representatives, in a ceremony held on 10 January 2018.

The National Financial Education Strategy establishes a series of good practices for institutions that implement financial education programs. These include being transparent about the program objectives; prioritizing public objectives; teaching content such as regulation, saving, investment, and credit; developing financial competencies; and bearing in mind the need for periodic program evaluations.

Economics Up Close Contest

In the thirteenth version of the Bank's annual school contest, groups of high school students and their teachers were invited to answer the following question: "How does price stability contribute to the well-being of the community?" Entries are presented in a three-minute video.

The contest was kicked off on 15 March in the auditorium of the Regional Government of Araucanía, at a ceremony attended by about a hundred local students. This year, the Bank received 164 videos prepared by 523 students from 86 schools from all over the country. The videos were reviewed by 17 Central Bank economists, who chose the semifinalists. The final review was conducted by a panel of judges made up of Governor Mario Marcel; the Minister of Education, Adriana Delpiano; the Finance Minister, Nicolás Eyzaguirre: the Superintendent of Banks, Eric Parrado; Central Bank Board Member Rosanna Costa; former Governor Rodrigo Vergara; the Director of the National Institute for Youth, Nicolás Farfán; the Dean of the Economics Department of the University of Santiago, Jorge Friedman; and the winning teachers of the 2016 contest, Paulo Alegría and Aldo González.

The XIII version of the Economics Up Close contest was held in 2017

The winning groups were announced at an awards ceremony held on 15 November. In the eleventh and twelfth grade category, first place was awarded to the team from the *Liceo Camilo Henríquez* in *Temuco*. Second place went to the *Instituto Superior de Comercio Enrique Maldonado Sepúlveda* in *Talca*; third place, to the Thomas Jefferson School in *Concepción*. In the ninth and tenth grade category, first place was awarded to the Redland School in *Las Condes*; second place, to the Lincoln International Academy in *Lo Barnechea*; and third place, to the *Instituto Santa María* in *San Carlos*.

D.5 Regional Visits

Regional meetings are intended to promote the public's learning and familiarity with the Bank's objectives, policies, instruments, and forecasts; to facilitate a better understanding of the Bank's actions; and to improve the effectiveness of its policies.

Over the course of the year, the Bank, in conjunction with a regional university or trade association, organizes a number of meetings to present the *Monetary Policy Report* and the *Financial Stability Report*, together with complementary information specific to the region. The people who attend these presentations have a wide range of backgrounds, including the business world, academia, government, trade associations, and productive sectors.

In April, a total of six regions were visited to present the March *Monetary Policy Report*. On Tuesday, 4 April, the Governor gave the presentation in *Copiapó*, at the regional meeting organized with the Copiapó office of the Chilean Chamber of Construction (CChC), while Board Member Pablo García gave a talk to academics, businessmen, and students in *Concepción*, in an event organized in conjunction with the University of *Bío-Bío*.

Board Member Pablo García presents the two reports in *Punta Arenas,* at a seminar entitled "The Variables That Will Characterize 2017."

On the same day, Board Member Joaquín Vial presented the Monetary Policy Report in *Osorno* and then traveled to *Puerto Montt* to give the presentation at a seminar attended by businessmen and executives from in and around the city. Both events were organized by the Manufacturing Development Association (Sofofa).

In *Arica*, Deputy Governor Sebastián Claro spoke at a seminar on Friday, 7 April, which was organized in conjunction with the Regional Development Corporation of *Arica and Parinacota* (Cordap). Finally, Board Member Rosanna Costa spoke at a meeting of the Progress Board in *Maule*.

In the week of 5–9 June, the Bank's Governor and Board Members presented the June *Monetary Policy Report* and the *Financial Stability Report* for the first half of 2017 in Santiago and in four regions of the country.

On Tuesday, 6 June, Board Member Pablo García gave a presentation on the two reports in *Punta Arenas*, at a seminar entitled "The Variables That Will Characterize 2017." The event was organized by Sofofa.

The next day, Board Member Rosanna Costa presented the *Monetary Policy Report* and the *Financial Stability Report* to businessmen and executives from the *Biobío* Region, in the city of *Chillán*, at a regional meeting coordinated in conjunction with the *Chillán* office of the CChC. On Friday, 9 June, Governor Mario Marcel gave a talk on the two publications in *Iquique*, at an event organized with the Iquique Duty Free Zone (Zofri). On the same day, Board Member Joaquín Vial presented the reports in *Calama*, at a meeting organized in coordination with the *Calama* office of the CChC.

In September, the Bank visited four regions to present the *Monetary Policy Report*. Board Member Pablo García spoke at a conference in *La Serena* on Thursday, 7 September, at an event organized in

conjunction with the Catholic University of the North. On Friday, 8 September, Board Member Joaquín Vial presented the report in *Temuco*, at a seminar organized in coordination with *Corparaucanía*; Board Member Rosanna Costa spoke in *Valdivia*, at a meeting organized with the Austral University of Chile; and Deputy Governor Sebastián Claro, presented the report in *Concepción* at a seminar organized by Sofofa.

On Tuesday, 5 December, Board Member Joaquín Vial presented the *Monetary Policy Report* and the *Financial Stability Report* for the second half at an event organized by Sofofa in *Viña del Mar*; and Board Member Rosanna Costa gave a talk at a seminar organized in conjunction with the Austral University, at the *Puerto Montt* campus. On Thursday, 7 December, Governor Mario Marcel gave a presentation on the two reports in *Arica*, at a meeting organized by Sofofa.

E. MISCELLANEOUS

E.1 Technological Changes

Cyber-security and information security were key priorities in 2017. An international consultant specializing in technological security was hired to provide support for the Bank's review of different aspects of technological security. In this context, a work plan was developed to allow the Bank to continue improving its security levels and resistance to cyber-security threats.

The Bank also began the application of recommendations in the SWIFT Customer Security Program (CSP), which involves changes in the technological architecture and operating procedures in order to align with industry best practices in security.

A series of diffusion and awareness campaigns was developed for staff on best practices in information security, which included a number of tests and drills.

With regard to equipment, the Bank continued its modernization program in 2017, updating the platform used for managing remote user access. Progress was also made on centralized security management of mobile devices and load balancing between processing sites. In addition, computer equipment for the central server platform and user systems was upgraded due to technological obsolescence.

Another project launched in the year was the replacement, due to obsolescence, of the Bank's analogue telephone system, with the implementation of a new unified communications solution that integrates telephone services, messaging services, and video conferences on a single platform.

Progress also continued on the migration of legacy applications to more modern development platforms, so as to extend their continuity and support and incorporate new and more powerful features.

Finally, the Information Systems Management participated actively in a series of technological projects initiated in the user areas of the Bank, including the implementation of the second phase of the new open market operations system, which incorporated new instruments and features on the platform; the start-up of the integrated Treasury Information System (TIS) to manage the distribution of cash;

Bilateral meeting between the Central Bank and the International monetary Fund (IMF).

The Governor of the Central Bank of Chile, Mario Marcel, with Governor of the Palestine Monetary Authority, Azzam Shawwa.

The Governor of the Central Bank of Chile, Mario Marcel, and The Governor of the Bank of Spain, Luis María Linde, sign a cooperation agreement between the two institutions.

and the definition of the technological architecture that will support the new international reserve management solution.

E.2 External Auditors

The second paragraph of Article 76 of the Basic Constitutional Act stipulates that the Central Bank's financial statements must include an independent auditors' opinion and that the Board is to appoint the auditors from among those registered with the Superintendence of Banks and Financial Institutions (SBIF). After issuing a call for tenders to contract financial statement auditing services for an initial period of three years, with a maximum of three contract renewals, and based on a favorable report by the Audit and Compliance Committee, the Board awarded the contract for professional auditing services for the period 2014–2016 to *KPMG Auditores y Consultores Ltda.*, via Resolution 1,775 of 5 September 2013; the contract can be automatically renewed annually in the 2017-2019 period.

E.3 International Relations Activities

In 2017, the Bank maintained both its regular international activities and a wide range of additional activities. The former included the bimonthly and annual meetings of governors of members of the Bank for International Settlements (BIS); the BIS meeting of alternate governors; the spring and annual meetings of the International Monetary Fund (IMF); the annual meeting of the Inter-American Development Bank (IDB); the meetings of central bank governors of South America (formerly Mercosur and associated countries); the Meeting of Central Bank Governors of Cemla and of the Cemla Committee of Alternates; the meetings of the Institute of International Finance (IIF), held in conjunction with the annual IDB meeting and the annual IMF meeting; and the IMF Article IV mission.

Additional activities in which the Bank participated included international seminars, conferences, and meetings held both in and outside Chile, official visits from foreign authorities, missions from international organizations, and technical visits by delegations from other central banks.

In Chile, David Shrier, the Managing Director of MIT Connection Science, gave a presentation on Current Trends in FinTech and Big Data; the Bank hosted the twelfth meeting of the Regional Consultative Group for the Americas of the Financial Stability Board (FSB); IMF economists presented the Regional Economic Outlook (REO) Report; and Gian Maria Milesi-Ferretti, the Deputy Director in the IMF Research Department, presented a chapter of the World Economic Outlook (WEO) to Bank staff and guests.

The official visits by foreign authorities featured the Governor of the Palestine Monetary Authority, Mr. Azzam Shawwa, and the Governor of the Bank of Spain, Mr. Luis Linde. The latter visited the Central Bank in November to give a talk on monetary policy in the European Unión and the evolution of the Spanish economy and to sign a cooperation agreement with the Bank. The agreement establishes and regulates work programs including short-, medium-, and long-term visiting positions in different areas, as well as other forms of technical cooperation between the two Banks, to promote the exchange

of knowledge and experience on central banking issues. The agreement renews and strengthens an agreement in place between the two Banks since 2002, which has provided multiple training opportunities on technical and other central banking issues.

The Bank also signed staff exchange programs with the Bank of South Korea, the OECD, and the BIS Representative Office for the Americas (Mexico). In the case of South Korea, the Bank welcomed a senior economist from the country's central bank to work in the Economic Analysis and Modeling Area for six months. In the cases of the OECD and the BIS Regional Office, the Bank sent two economists abroad for a period of two years.

Technical visits to the Central Bank included delegations from the Reserve Bank of Australia, the Central Bank of Argentina, Bundesbank, the Central Bank of Uruguay, the Central Bank of the Dominican Republic, and the London School of Economics.

The Governor of the Central Bank gave a presentation on the Chilean economy to the Latin American Chamber of Commerce in Zurich, Switzerland, covering recent developments and future challenges; conducted a road show in New York, United States, during which he met with top executives of the main investment banks and with William C. Dudley, President of Federal Reserve Bank of New York; participated as a panelist for a round table organized by the School of International and Public Affairs (SIPA) at Columbia University in New York; gave a presentation for Chile Day in London; delivered a talk on Chilean Monetary Policy in the International Context at the London School of Economics; and was a keynote speaker at the annual conference of the Cambridge Centre For Alternative Finance (CCAF) at the University of Cambridge, United Kingdom, where he discussed FinTech and the future of central banks from a Latin American perspective.

E.4 Access to Information

Law on Transparency

With regard to compliance with the active transparency requirements established in Article 7 of Law 20,285 on public access to information and in Board Resolution 1472-01-090416, the Transparent Bank web section was reorganized in 2017, so as to give the public easier access to all the information that the Bank makes available, in compliance with the legal provisions on public access to information, probity in public service, and lobbying and special interests, as well as other good practices in transparency that the Bank has implemented, such as the Board Agenda.

In addition, the publication of information required under paragraph (e) of the aforementioned Article 7, which covers contracts for the supply of movable goods or services, was modified to adopt the standard used by government agencies in terms of the content that is published and how it is made available to the public. Thus, the Active Transparency web section now incorporates a link to the list of current contracts by year.

Another important decision adopted by the Board in the area of transparency was to make available to the public, on the website, the full records of the monetary policy meetings after ten years, starting in March 2018. The first publication will include all the records for meetings held from 2000 to 2007.

In 2017, the Bank received 73 applications for access to information, in accordance with the provisions of Law 20,285 on public access to information, which represents a decrease from 2016 (82). These requests were addressed within the time allowed under Article 14 of the law, which is 20 business days from the date the application is received.

No complaints have been filed against the Bank to date in the Santiago Court of Appeals, in accordance with the provisions of Sections 65 bis and 69 of the Bank's Basic Constitutional Act.

Law on Lobby

Law 20,730, which regulates lobbying and the representation of special interests to public authorities, is applicable to the Central Bank of Chile, and it establishes that the Governor, the Deputy Governor, and the other Board Members are subject to the obligations stipulated therein. The law further establishes that the legal obligations can be extended to other functionaries via Board Resolution, if their duties, responsibilities, or position within the Bank require that they be subject to the regulatory guidelines, if they possess substantial decisionmaking power, or if they are in a position of significant influence over others who do.

The full list of Central Bank authorities who are to be considered subject to this law, including their names and positions, can be found on the Bank's website.

In 2017, the Central Bank authorities subject to the law had 225 meetings with lobbyists and special interest representatives, 109 business trips, and 165 donations or gifts received.

All of this information was published on the Central Bank's website, in the transparency and probity section, and on the Infolobby website of the Transparency Board, as specified in the Agreement signed on 25 May de 2015.

Law on Probity

Law 20,880, on Probity in Public Service and the Prevention of Conflicts of Interest, regulates the obligation of public authorities and functionaries to publicly declare their interests and equity. This obligation is applicable to the Board Members and General Manager of the Central Bank of Chile, in accordance with the terms established by the law and the provisions on the declaration of conflicts of interest, personal interests, and equity of Section 14 of the Bank's Basic Constitutional Act.

The current conflict-of-interest statements submitted by the Bank's authorities in 2017 are published on the organization's website, in the transparency and probity section, and on the Transparency Board's website (www.Infoprobidad.cl).

Exchange of information

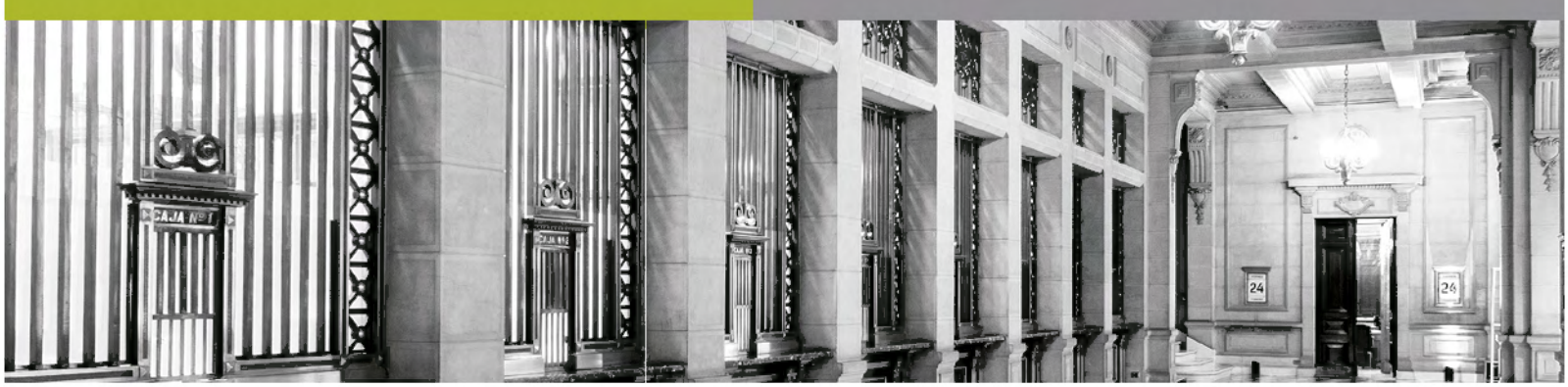
Coordination with other institutions

Good practices

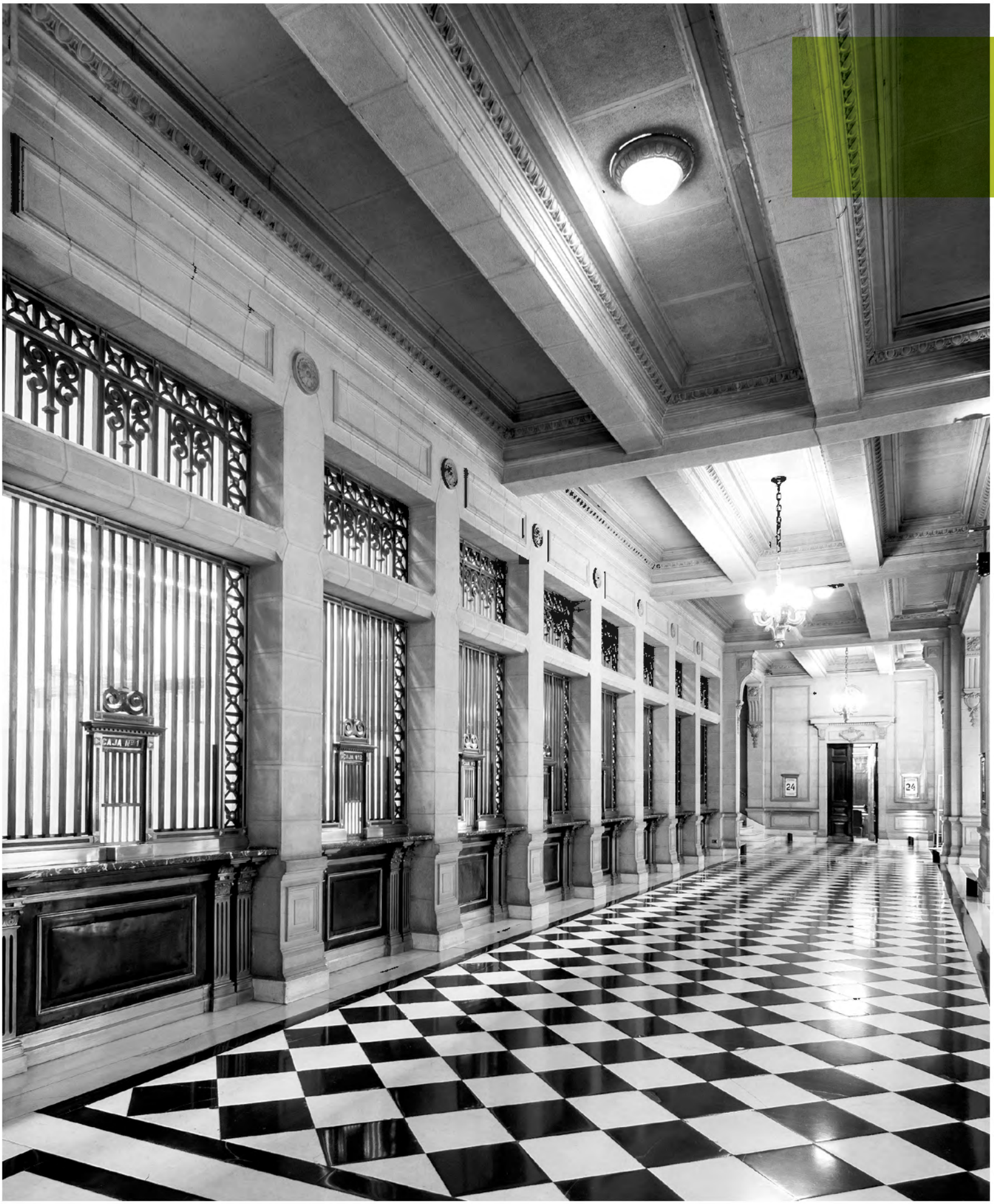
Risks and opportunities

knowledge development

Technological changes



APPENDICES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Appendix I
PRESS RELEASES ON MONETARY POLICY MEETINGS IN 2017

19 JANUARY

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to lower the monetary policy interest rate by 25 basis points, to 3.25%.

Internationally, global financial conditions have improved, and emerging market asset prices have increased. Copper and oil prices, while fluctuating, have stayed above the level of mid-2016. Output data confirm a better performance in the developed world and greater weakness in Latin America.

Domestically, monthly CPI inflation surprised to the downside, which brought annual inflation to 2.7%. Inflation expectations are around the target toward the end of the forecast horizon, although they are in the lower part of the range for the coming months. Output data continue to point to a weak performance, this time concentrated in non-natural-resource sectors. Demand indicators show growth rates in line with past quarters, and the labor market is also following its previous trend. Long-term interest rates have returned to the levels recorded before the U.S. election.

As indicated in the last *Monetary Policy Report*, the Board considers that if recent trends in the economic scenario continue, together with their implications for the medium-term inflation outlook, it will be necessary to increase the monetary stimulus. The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon.

14 FEBRUARY

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 3.25%.

Internationally, global financial conditions continue to improve, and emerging market asset prices continue to rise, with a particularly good performance in economies in the region. The copper price increased, in part due to supply factors. The oil price is around the same level of a month ago. The data continue to point to a recovery of global output, especially in the developed world, although there are still significant risks.

Domestically, annual inflation reached 2.8%, consistent with the forecast in the *Monetary Policy Report*. Inflation expectations are around the target toward the end of the forecast horizon, although they are in the lower part of the range for the coming months. Output and demand data continue to show a weak performance, and the labor market continues to follow its previous trends. Long-term interest rates fell, and the peso appreciated.

The Board considers that, in the most probable scenario, it will be necessary to increase the monetary stimulus in the short term. The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon.

16 MARCH

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to lower the monetary policy interest rate by 25 basis points, to 3%.

Internationally, global financial conditions remain favorable. In the developed world, the data continue to point to a higher growth and inflation scenario. In this context, expectations for monetary policy normalization increased, especially in the United States. Commodity prices fell, in particular the oil price. Important risks remain.

Domestically, annual inflation was 2.7%, in line with the forecast in the December *Monetary Policy Report*. Inflation expectations are around the target toward the end of the forecast horizon, although they are in the lower part of the range for the coming months. Output and demand data continue to show a weak performance. In the labor market, the deterioration of wage employment intensified, although the unemployment rate remained stable.

The Board considers that the recent trends in the macroeconomic scenario, together with their implications for the medium-term inflation outlook, could require an additional increase in the monetary stimulus. The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon.

13 APRIL

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to lower the monetary policy interest rate by 25 basis points, to 2.75%.

Internationally, global financial conditions remain favorable, and various indicators point to a higher growth and inflation scenario in the developed world. Commodity prices were mixed, with an increase in the oil price. Significant risks remain.

Domestically, inflation and output data were in line with projections in the March *Monetary Policy Report*. Annual inflation held at 2.7%, inflation expectations are around the target toward the end of the forecast horizon. Output and demand data continue to show a weak performance. The labor market deteriorated somewhat more than expected.

To ensure the convergence of inflation to the target, the Board will evaluate the need for an additional increase in the monetary stimulus. Any adjustment will depend on the medium-term inflation outlook. As always, the Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon.

18 MAY

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to lower the monetary policy interest rate by 25 basis points, to 2.5%.

Internationally, financial conditions remain favorable despite some volatility, and the data point to a higher growth scenario in the developed world. Commodity prices were again mixed, with a drop in the copper price. Significant risks remain.

Domestically, annual inflation held at 2.7%, and inflation expectations are around the target toward the end of the forecast horizon. The national accounts for the first quarter showed an output and demand scenario in line with March *Monetary Policy Report,* reflecting the negative impact of mining and construction. Private consumption remains stable, in line with the evolution of the labor market.

The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon. Future changes in the MPR will depend on internal and external macroeconomic conditions and their implications for inflation expectations.

15 JUNE

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5%.

Internationally, the data continue to show favorable financial conditions and a gradual recovery of output in the main developed economies, in line with the description in the *Monetary Policy Report*. Commodity prices were mixed, with a drop in oil and oil derivatives prices.

Domestically, annual inflation was 2.6%, and inflation expectations are around the target toward the end of the forecast horizon. Partial output and demand data for the second quarter are consistent with the forecast, reflecting the negative impact of mining and construction. Private consumption remains stable, in line with the evolution of the labor market.

The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon. Future changes in the MPR will depend on internal and external macroeconomic conditions and their implications for inflation expectations.

13 JULY

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5%.

Internationally, long-term interest rates rose, but financial conditions remain favorable. In general, the news was consistent with a gradual recovery of global output. The copper price increased, while the oil price is around the level of a month ago, albeit with some fluctuation.

Domestically, the main news was monthly inflation of -0.4% in June, largely due to fresh fruit and vegetable prices and some other specific product prices. Consequently, annual inflation dropped to 1.7%. Inflation expectations have fallen at the shortest terms, but they remain around the target toward the end of the forecast horizon. Partial output and demand data for the second quarter are consistent with projections, reflecting the negative impact of mining and construction. The growth of private consumption was stable, in line with the evolution of the labor market.

The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon. Future changes in the MPR will depend on internal and external macroeconomic conditions and their implications for inflation expectations.

17 AUGUST

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5%.

Internationally, the news continued to point to a favorable scenario. The global growth outlook has strengthened, and global financial conditions remain expansionary. In general, commodity prices increased, most notably the copper price.

Domestically, July inflation was 0.2%, such that annual inflation held at 1.7%, which is below the forecast in the last *Monetary Policy Report*. Inflation expectations are largely unchanged. In the second quarter, GDP growth was weak, reflecting the performance of some investment-related sectors and one-off factors. Private consumption remains stable, in line with the evolution of the labor market, and expectations are less pessimistic. The peso has appreciated.

The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon. Future changes in the MPR will depend on internal and external macroeconomic conditions and their implications for inflation expectations.

14 SEPTEMBER

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5%.

Internationally, the financial markets were somewhat more volatile, in a context in which global financial conditions remain favorable and the U.S. dollar has weakened. The world growth outlook remains positive. Commodity prices increased in the past month, including copper, which partially reversed the most recent decline.

Domestically, August inflation was in line with the forecast in the last *Monetary Policy Report*, bringing annual inflation to 1.9%. Inflation expectations have fallen at the shortest terms, incorporating the effect of the peso appreciation, but they remain around 3% in two years. With regard to growth, consumption-related activities continue to record a relatively better performance than investment-related sectors. Private consumption is in line with the evolution of the labor market, and expectations have become slightly less pessimistic.

The data released since the publication of the September *Monetary Policy Report* are consistent with the baseline scenario and the respective monetary stimulus—that is, with the MPR remaining around its current level and then beginning to rise toward its neutral level only after the economy begins to close the output gap. The balance-of-risk assessment has not changed. In particular, the risks to output and inflation are broadly balanced in the medium term, but with a downward skew for inflation in the short term. As always, the Board will watch for deviations from the baseline scenario that could affect the convergence of inflation to 3% in the two-year horizon and thus justify adjustments in the MPR.

19 OCTOBER

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5%.

Internationally, global output and the world growth outlook have not changed significantly, with continuing signs of increased dynamism. Global financial conditions remain favorable. The biggest news of the month was the increase in some commodity prices, in particular copper and oil.

Domestically, the September CPI inflation surprised to the downside, which brought annual inflation down to 1.5%. While inflation expectations fell significantly at the shortest terms, only minor adjustments were seen at longer terms. The data available for the third quarter show that the evolution of output and demand are in line with the baseline scenario of the *Monetary Policy Report*, and consumption-related activities continue to record a better relative performance than investment-related sectors. Private consumption continues to evolve in line with the labor market, and expectations have become less pessimistic.

The output data released since the publication of the September *Monetary Policy Report* are consistent with the baseline scenario and the respective monetary stimulus. However, the recent inflation data suggest that inflation will be lower than expected in the short term, which could delay convergence to the target in the two-year horizon. The Board will closely monitor this risk, identified in the *Monetary Policy Report*, as the materialization of this scenario could require an adjustment in the MPR. At the same time, the Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon.

14 NOVEMBER

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5%.

Internationally, third-quarter output data are consistent with a more dynamic scenario. Global financial conditions have not changed significantly. The oil price has increased in the recent weeks, while the copper price fell slightly, although it remains above the forecast.

Domestically, October inflation was higher than expected, at 0.6%, partially reversing the negative surprise of September. Consequently, annual CPI inflation increased to 1.9%. Short-term inflation expectations remain low, while medium-term expectations have not changed. Output and demand data for the third quarter are in line with the baseline scenario of the *Monetary Policy Report*. Private consumption continues to evolve in line with the labor market, and expectations have become less pessimistic. Investment remains weak, reflecting the performance of construction.

The output data released since the publication of the September *Monetary Policy Report* are consistent with the baseline scenario and the respective monetary stimulus. However, inflation will remain low in the short term, which could delay convergence to the target in the two-year horizon. The Board will closely monitor this risk, identified in the *Monetary Policy Report*, as the materialization of this scenario could require an adjustment in the MPR. At the same time, the Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon.

14 DECEMBER

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5%.

Internationally, GDP data continues to indicate a synchronized recovery in the developed world, although inflation levels remain low. Monetary policies are evolving in line with expectations. In this context, global financial conditions have not changed significantly. Commodity prices have been mixed, with the copper price fluctuating around a somewhat lower level than a month ago.

Domestically, CPI inflation increased 0.1% in November, keeping annual inflation at 1.9%. CPIEFE inflation decreased 0.1%; annual core inflation thus declined to 1.8%. Inflation expectations did not change significantly. Output and demand data for the early fourth quarter are consistent with the baseline scenario of the *Monetary Policy Report* and continue to reflect the weak performance of non-mining activity and sectors tied to construction investment. Consumer and business expectations have not changed significantly. In the labor market, self-employment remains dynamic, while wage employment is weak. The peso and other financial variables have been fairly stable in the month.

The output data released since the publication of the September *Monetary Policy Report* are consistent with the baseline scenario and the respective monetary stimulus. However, there is still a risk that the persistence of the current low inflation rate could delay convergence. If necessary, the Board will act quickly to adjust the monetary stimulus. The Board reaffirms its commitment to being flexible in its monetary policy conduct, in order to keep forecast inflation at 3% in the policy horizon.

APPENDIX II
PRESS RELEASES ON FOREIGN EXCHANGE AND FINANCIAL MEASURES IN 2017

4 JANUARY

At its meeting on 20 December 2016, the Board of the Central Bank of Chile approved the annual auction calendar for 2017, pursuant to which no new bonds will be issued in the year.

The scheduled debt maturities for 2017 are equivalent to Ch$1.700 trillion. Of this, $950 billion will be absorbed through Central Bank discount promissory notes (PDBC), in order to adequately manage liquidity in the local market. The difference corresponds mainly to the growth of the monetary base.

This auction schedule is subject to modification in the event of significant changes in market conditions. If that occurs, the changes will be announced in due time.

11 JANUARY

The Central Bank of Chile has modified Chapter XIV of the *Compendium of Foreign Exchange Regulations* and Chapters I and XIV of the *Compendium's Procedures and Forms Manual*, to facilitate the operation of international custodians in the country. The changes take into account the general orientation of the government's economic policy and safeguard compliance with foreign exchange regulations.

The changes have to do with the foreign exchange information required on overseas investments channeled through international custodians or international securities depositories. These entities are financial infrastructures that provide securities custody or deposit services to investors who may or may not be domiciled in or resident of the country in which the instruments are traded.

The new regulations establish that foreign exchange operations involving overseas investors, as defined in Chapter XIV of the *Compendium*, in which an international custodian acts, in its own name, on the account of people who are not domiciled in or resident of Chile, can be reported using the tax identification number (RUT) assigned to the international custodian, in accordance with current tax regulations.

The foreign exchange regulations further establish that the international custodian is obligated to report periodically to the Central Bank, providing a disaggregated list of investments in local financial instruments that it holds in custody on the account of investors who are not domiciled in or resident of Chile. This information will be useful for statistical purposes and for monitoring financial stability, in fulfillment of the Bank's institutional objective.

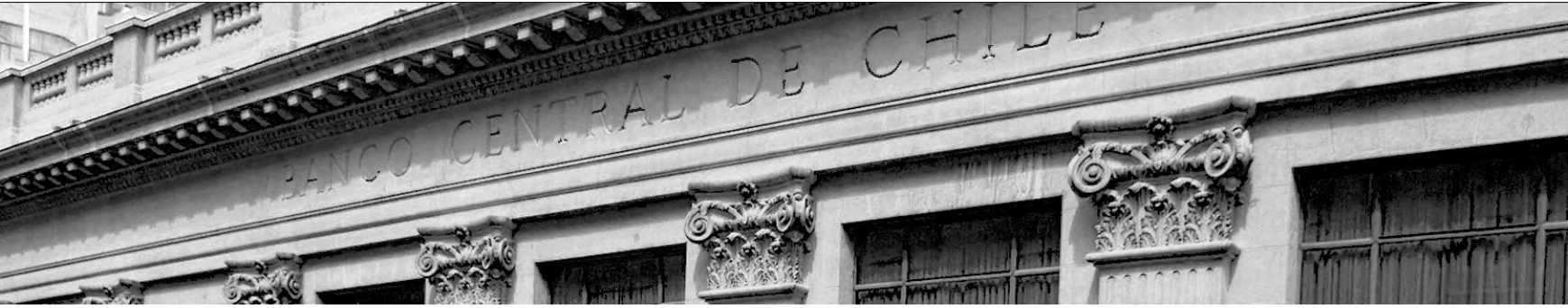
The regulatory modifications were open for public consultation from 24 November to 9 December 2016, during which time the Bank received comments and suggestions from local and international agencies, several of which were incorporated into the final version of the text. A summary of the main comments received during the public consultation and the corresponding responses can be found on the Central Bank's website.

30 JANUARY

The Central Bank of Chile announces the entry into force of modifications to the withholding tax on bond interest subject to Article 104 of the Income Tax Law.

Law 20,956, which establishes measures to boost productivity, incorporates modifications to the Income Tax Law, including adjustments to the tax scheme applicable to bonds subject to Article 104 of the Income Tax Law, in effect as of 1 February 2017.

With regard to bonds issued by the Central Bank of Chile that are subject to Article 104 of the Income Tax Law, as of 1 February 2017, the Bank must withhold 4% of interest earned at the time the coupon is paid. For bonds issued before that date, the first withholding and payment will be applied



only to interest earned after the entry into force of the aforementioned regulation.

The new withholding rule does not imply a change in the general conditions on bonds issued by the Central Bank of Chile, but rather reflects compliance with a mandatory obligation imposed by the tax legislation.

1 MARCH

The Board of the Central Bank of Chile decided to increase the overseas investment limit for insurance and reinsurance companies, from 20 to 30% of their technical reserves and risk-based capital, pursuant to the provisions of Law 20,956, which establishes measures to boost productivity.

This new legislation modified Statutory Decree (DFL) 251 on Insurance Companies, eliminating the ceiling of 20% of technical reserves and risk-based capital. It is the duty of the Central Bank of Chile to implement this change and to establish, with prior approval from the Superintendence of Securities and Insurance (SVS), the maximum overseas investment limit for insurance and reinsurance companies.

The objective of the Executive Office in promoting this legal modification was to promote "greater diversification and liquidity in the companies' investment portfolio, which is hoped will translate into better pensions from the life insurance companies and an increase in the financing available for infrastructure works."

In accordance with this new legal framework, and taking into account both the general orientation of the government's economic policy and the Bank's institutional mandate, the Board modified Chapter III.F.6 of the *Compendium of Financial Regulations* to increase the overseas investment limit for insurance and reinsurance companies.

To ensure that these adjustments in the insurance companies' investment portfolios do not affect the normal functioning of the internal or external payment systems, and to minimize the risk of possible adverse effects deriving from large portfolio shifts, the limit will be increased gradually, via two successive increases of 5% each, with the first taking effect today and the second on 1 September 2017, so as to arrive at the new 30% limit.

This modification has been approved by the SVS and was opened to public consultation, during which comments were received from various agents in the financial sector.

Finally, the Central Bank of Chile has the legal authority to revise this limit in the future, making necessary adjustments as circumstances merit, with prior approval by the SVS.

30 JUNE

Law 20,950 authorizes nonbank entities to issue prepaid debit cards and charges the Central Bank of Chile with issuing the applicable regulations to the companies that issue and operate the cards. In fulfilling this duty, the Bank has decided to undertake a comprehensive review of its regulations on retail payment instruments, in order to update and systematize the current regulatory framework, taking into account current market developments and safeguarding the security and efficiency of the retail payment system.

In March of this year, the Bank published the proposed regulations on the issue and operation of prepaid debit cards for public consultation. The process generated over 220 comments, which contributed to improving the new regulations. A large share of the suggestions were incorporated into the final version of the text.

In addition to establishing a regulatory framework for nonbank firms that issue prepaid debit cards, the new regulations incorporate a set of modifications aimed at increasing the supply of services to companies in the payment network. Most notably, the regulations explicitly allow the development of a four-party model, in which the issuer and the acquirer are not necessarily directly related, which should facilitate the supply of operation services to businesses and other entities in the payment network.

Many of the comments received in the public consultation expressed approval of the changes in general, while also indicating a number of specific areas for improvement. In accordance with the Central Bank of Chile's guidelines for this type of process, a summary of the main comments, and the Bank's response, has been published.

As a result of the public consultation, the following changes were incorporated, based on the comments received:

i. Adjustments to the algorithms for calculating the capital requirements of credit and prepaid card issuers.

ii. Authorization of new modalities for loading and using prepaid cards, including electronic transfers and ATM withdrawals.

iii. Change in the nomenclature, to replace the term Business Service Providers with Payment Processing Service Providers (PPSP); and an increase in the transaction limit that can be settled without having to register as an Operator.

iv. Modifications to the definition of Card Operators, allowing PPSPs to authorize and record transactions and thus limiting the definition of Operator exclusively to the clearing of payments for affiliated entities. The Issuers and Operators that delegate authorization and recording to a PPSP must report the decision to the Superintendence of Banks and Financial Institutions (SBIF) and treat these entities as critical suppliers.

The Bank received a number of comments related to free competition in this industry. The regulations issued by the Bank incorporate general principles and requirements that contribute to this objective, within the framework of the Bank's authority and powers. There are, however, a number of aspects that exceed the Bank's authority and thus will need to be addressed at the legal level or submitted for consideration by the entities specially charged with the defense of free competition.

Finally, as indicated in March, in accordance with its legal mandate to safeguard the normal functioning of the internal and external payment systems, the Central Bank of Chile aims to contribute to the expansion of the retail payment market so that a larger share of the population can benefit from the use of electronic payment instruments, under adequate security conditions for the different economic agents involved in their operation. The new regulations issued by the Bank are effective as of their publication in the *Official Gazette* on Friday, 30 June. However, some specific requirements will enter into force at a later date as stipulated in the transitional provisions, subject to the issue of the necessary instructions on implementation and compliance by the SBIF.

18 AUGUST

In light of its institutional mandate and the general orientation of the government's economic policy, the Central Bank of Chile has decided to expand the category of recognized external formal secondary markets to include jurisdictions with a sovereign rating of A and BBB and which also are on the SVS list of recognized markets, in accordance with SVS regulations (NCG N° 352).

This regulatory modification has been reviewed and approved by the Superintendence of Pensions.

Previously, Central Bank regulations stipulated that eligible overseas formal secondary markets were restricted to foreign securities or futures exchanges in countries with a sovereign rating equivalent to AA- or higher. Under this regulation, eligible exchanges must also be approved by the Credit Rating Commission.

This modification was open for public consultation from 28 July to 11 August, during which the only comment received was a request from the Central Securities Depository to clarify the general regulations on the custody of pension fund investments. After reviewing the content and scope of the comment, the decision was made to maintain the text of the regulation as published, given that the requested clarification is provided in Chapter III.F.1 of the *Compendium of Financial Regulations*.

11 OCTOBER

In accordance with the authority granted to the Central Bank of Chile under Law 20,956, the following structural limits on investment in alternative assets are established for the pension funds and the Solidarity Unemployment Fund (SUF).

— For the pension funds, alternative asset investment limits are defined by type of fund, as a percent of the total value of the fund, as follows:

Type A	Type B	Type C	Type D	Type E
10%	8%	6%	5%	5%

- For the Solidarity Unemployment Fund, the alternative asset investment limit is 5% of the value of the fund.

Although Law 20,956 allows the Bank to set these limits within a range of 5–15% of the total value of the corresponding fund, the limits were ultimately set below the upper limit of the range for all types of funds. In making this decision, the Board considered that the pension funds' portfolio adjustments should be executed without affecting the normal functioning of the financial system.

These limits will be incorporated into Chapters III.F.4 and III.F.7 of the Bank's *Compendium of Financial Regulations* as of 1 November 2017.

This modification was open for public consultation from 15 September to 3 October 2017, inclusive. Comments were received from the Chilean Association of Investment Fund Managers (*Asociación Chilena de Administradoras de Fondos de Inversión A.G.*) and *AFP Capital*. Both organizations suggested setting higher limits than proposed by the Central Bank, arguing that a larger cushion would allow the funds to attain higher returns, as suggested by the available international evidence. However, the Central Bank deemed that the arguments and evidence presented were not sufficient to justify modifying the proposal submitted for public comment, given that the Bank's initial decision took this evidence into account, together with concerns for financial market stability.

As indicated when the public consultation was opened, the Bank will consider the possibility of raising the limits within the legally established range in the future, based on its monitoring of the financial markets and pension fund investments after the regulation has been implemented.

15 DECEMBER

The Board of the Central Bank of Chile announces that as of today, it is adopting extraordinary measures to facilitate the normal functioning of the foreign currency money market and interbank liquidity in foreign currency, which have tightened due to an increased use of currency hedging operations.

The following measures will be implemented starting next week:

(1) A dollar swap program, with up to US$500 million available during each auction. This is a temporary program that will be available for four weeks, with a total of eight auctions in the period. The swaps will have a maturity of 30 day.

(2) To complement the above program and offset its monetary effects, the Bank will offer repo operations to inject liquidity in pesos, at the same maturity and in the same period as the dollar swap program. This is a collateralized repo program offered through the traditional liquidity window, with eligible collateral defined as PDBC, BCU, BCP, BTU, and BTP securities.

The Central Bank of Chile will continue to closely monitor the evolution of the markets and will move quickly to adopt further measures as needed.

29 DECEMBER

Following a public consultation on the new Chapter III.H on Payment Systems in the *Compendium of Financial Regulations*, and with the prior approval of the Superintendence of Banks and Financial Institutions (SBIF), the Board of the Central Bank of Chile approved the new regulations yesterday, via Resolution 2119E-01-171228.

Specifically, the new Chapter adopts the Principles for Financial Market Infrastructures (PFMI), expressly requiring their application in the real-time gross settlement (RTGS) system managed by the Bank (Chapter III.H.4 of the *Compendium*) and the large-value domestic-currency clearing house (Chapter III.H.5 of the *Compendium*), managed by the *Sociedad Operadora de la Cámara de Compensación de Pagos de Alto Valor S.A. (Combanc S.A.).*

As explained when the public consultation was opened, adhering to the PFMIs implies formalizing practices that are already in use in the Chilean financial system. In this sense, the main value of this initiative lies in explicitly recognizing, in the Central Bank's regulations, a commitment to following and enforcing a wide set of internationally accepted standards.

During the consultation period for the regulation, from 15 to 22 December, the Central Bank received a request for clarification from the Association of Banks and Financial Institutions (ABIF) regarding the scope of the

application of these guidelines in banking entities. In response, the Bank specified that the approved regulation only applies to banks and financial institutions that are supervised by the SBIF in terms of their participation in the payment systems that are now required to comply with the PFMIs, as stipulated in the regulation. Thus, the aforementioned participants are subject to supervision in this area by the Superintendence, but the regulation does not extend to other areas of the banks' business, such as contracts, products, and customer relations.

This regulation was submitted to the SBIF for prior approval, as required under Section 35 of the Bank's Basic Constitutional Act. In its report, the SBIF stated that it agrees with the spirit of the new regulation and reiterated its commitment to adhering to the PFMIs and ensuring compliance by the market infrastructures subject to its supervision. At the same time, the report included some suggestions for improving the text, mainly in terms of establishing a more precise definition of situations that would be considered noncompliance with the regulation and the consequences thereof. A clarification was thus incorporated into the regulation, specifying that the aforementioned payment systems will not be considered in noncompliance if they are unable to comply with aspects of the PFMIs due to a reasons beyond their control, deriving from the current legal and/or regulatory framework.

The final text of the regulation approved by the Board incorporates these suggestions. It will be published in the *Official Gazette* on 4 January 2018, at which time it will enter into force.

The implementation of this regulation represents an important step toward fulfilling the commitment made in January 2017 by the Ministry of Finance, the Central Bank of Chile, the Superintendence of Banks and Financial Institutions, the Superintendence of Securities and Insurance, and the Superintendence of Pensions, whereby each authority will gradually implement the PFMIs in their respective regulatory and supervisory frameworks.

APPENDIX III
MAIN MEASURES TAKEN BY THE CENTRAL BANK OF CHILE IN 2017

JANUARY

4

The Bank reported that the Board, in its regular session on 22 December 2016, approved the Annual Debt Plan, which does not include any new bond issues in 2017.

10

Through Resolution 2029E-01-170110, the Bank modified Chapter XIV of the *Compendium of Foreign Exchange Regulations,* and its *Manual*, with regard to the foreign exchange information collected on overseas investments that are channeled through international securities depositories or custodians. The objective of the modification is to provide an alternative for foreign investors who do not have a Chilean tax identification number (RUT), obtained through the simplified procedure established by the Internal Revenue Service (Resolution 36), by allowing them to hold instruments representative of an investment made in Chile through an international custodian that does have a local tax identification number. The new regulation thus facilitates international custody operations involving securities issued in Chile, in line with the provisions of Law 20,956, which establishes measures to boost productivity, and with the general orientation of the government's economic policy.

19

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to reduce the monetary policy interest rate by 25 basis points, to 3.25% in annual terms.

FEBRUARY

9

Through Resolution 2040-02-170209, adopted pursuant to the provisions of Article 76 of the General Banking Law, the Central Bank authorized the *Banco de Crédito e Inversiones*, through its subsidiary City National Bank of Florida, to make an investment in the latter's second-tier subsidiary, City National Capital Finance, LLC, constituted in the United States of America.

14

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to hold the monetary policy interest rate at 3.25% in annual terms.

27

Through Resolution 2043E-01-170227, the Board modified Chapter III.F.6 of the *Compendium of Financial Regulations*, on overseas investment limits for insurance companies.

In accordance with the modifications introduced by Law 20,956 to Statutory Decree DFL 251 of 1931, the overseas investment limit for general and life insurance and reinsurance companies was gradually increased to 30% of technical reserves and risk-based capital. The objective is to promote greater diversification and liquidity in the companies' investment portfolios.

This regulatory modification was previously opened for public consultation through Resolution 2040-01-170209.

MARCH

16

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to reduce the monetary policy interest rate by 25 basis points, to 3% in annual terms.

27

Through Resolution 2051E-01-170327, on consideration of the agreement adopted at the *Banco de Chile* shareholders' meeting held on 23 March 2017, with regard to the distribution of dividends and the capital increase through the issue of bonus shares corresponding to 40% of 2016 profits,

the Central Bank Board dictated that all the earnings or surpluses due to the Central Bank, including the share of earnings earmarked for capitalization under the shareholders' agreement, shall be paid in cash. This decision was adopted in accordance with the stipulations of paragraph (b) of Article 31 of Law 19,396, on changing the form of payment of subordinated debt, and other applicable regulations.

APRIL

6

Through Resolution 2054-01-170406, the Board voted to authorize the brokerage firm MCC S.A. to operate in the formal exchange market, in accordance with the provisions of Chapter III of the *Compendium of Foreign Exchange Regulations.*

13

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to reduce the monetary policy interest rate by 25 basis points, to 2.75% in annual terms.

27

Through Resolution 2059-01-170427, to promote institutional transparency, the Board decided to release the methodology used by the Bank to calculate the observed exchange rate, which is published in accordance with Section 44 of the Bank's Basic Constitutional Act.

MAY

18

Through Resolution 2065-03-170518, the Board modified Chapter VI of the *Compendium of Foreign Exchange Regulations* to raise the commission on reimbursement requests processed by the Central Bank of Chile for authorized local institutions (banks) in association with the Aladi Reciprocal Payment and Credit Agreement, with regard to export operations whose payments are channeled through this mechanism via other central banks that are parties to the agreement. At the same time, temporary provisions were established for the application of the new commission.

18

At its monthly monetary policy meeting, the Board of the Central Bank of Chile reduced the monetary policy interest rate by 25 basis points, to 2.5% in annual terms.

26

Through Resolution 2067E-01-170526, the Board accepted the changes to the fiscal agency entrusted to the Central Bank through Executive Decree 2047 of 2015, modified by Executive Decree 423 of 2017, both issued by the Finance Ministry, to represent and act in the name and on the account of the General Treasury in the placement and total or partial prepayment of bonds representing direct public debt issued by the General Treasury in the local capital market, in one or more operations, in accordance with the amounts, mechanisms, rules, and dates established by instructions from the Finance Minister or a legally designated representative.

In accordance with this modification, the payments associated with the bond issue, service, or prepayment will be made directly by the General Treasury or an agent designated for this purpose. Furthermore, the payments associated with the bond service or prepayment for which the Bank has previously been designated fiscal agent will also be made directly by the General Treasury or an agent designated for this purpose, who will also maintain the respective records, and the Bank is thus relieved of any obligations previously designated to it in these cases.

30

Through Resolution 2068E-01-170530, the Board revoked the authorization of the brokerage firm *GBM Corredores de Bolsa Limitada* to operate in the formal exchange market, at the company's request.

JUNE

1

Through Resolution 2070-02-170601, the Board renewed the appointment of Mr. José Luis Cea Egaña as member and Chairman of the Central Bank's Audit and Compliance Committee, for a period of three years, effective 17 June 2017.

15

At its monthly monetary policy meeting, the Board of the Central Bank of Chile decided to hold the monetary policy interest rate at 2.5% in annual terms.

29

Through Resolution 2074-02-170629, the Board approved the new regulations on the issue and operation of credit, debit, and prepaid cards, which replace Section J of the *Compendium of Financial Regulations* in its entirety.

The changes represent a comprehensive revision of the regulations on payment cards, in order to incorporate recent market developments while safeguarding the security and efficiency of the payment systems. The changes also contain the necessary provisions for implementing Law 20,950, which authorizes nonbank entities to issue and operate prepaid debit cards.

The new regulations were previously opened for public consultation through Resolution 2047-01-170309.

JULY

6

Through Resolution 2075-01-170706, certain modifications were introduced to the Board's operating regulations, primarily in terms of the Bank staff that attends the Board's monetary policy meetings.

13

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to hold the monetary policy interest rate at 2.5% in annual terms.

AUGUST

10

Through Resolution 2083-02-170810, the Board appointed Mr. Marcus Cobb Craddock to replace Mr. Gonzalo Echavarría Martí as the alternate representing Mr. Francisco Ruiz Aburto, on the National Commission on Price Distortions described in Article 11 of Law 18.525.

17

Through Resolution 2084-01-170817, the Board approved a modification to Chapter III.F.3 of the *Compendium of Financial Regulations* on external formal secondary markets that are eligible for securities trading by the pension funds.

Specifically, the category of formal secondary markets has been expanded to incorporate foreign securities and futures markets located in jurisdictions with a sovereign rating of A or BBB (or the equivalent) by international credit rating agencies, based on the rating equivalencies established by the Risk Rating Commission under Decree Law 3500 of 1980. These markets must also be on the list of recognized markets maintained by the Superintendence of Securities and Insurance (SVS), in accordance with the applicable regulations (NCG 352).

This regulation was previously opened for public consultation through Resolution 2079-01-170728.

17

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to hold the monetary policy interest rate at 2.5% in annual terms.

22

Through Resolution 2085E-01-170822, the Board appointed Mr. Anthony Dawes Martindale as a full member of the Central Bank's Audit and Compliance Committee, for a period of three years, effective 22 August 2017.

SEPTEMBER

13

Through Resolution 2091E-01-170913, the Board put into effect an exceptional and temporary measure to increase to 40% the nonrefundable commission applicable to reimbursements and/or payments made by the Central Bank to authorized local institutions, deriving from exports from Chile whose payments are channeled through the Aladi Reciprocal Payment and Credit Agreement. This temporary increase is a preventive measure aimed at protecting the Bank's equity while the Central Bank of Venezuela's line of credit is being revoked.

14

At its monthly monetary policy meeting, the Board of the Central Bank of Chile held the monetary policy interest rate at 2.5% in annual terms.

15

Through Resolution 2093E-01-170915, the Board revoked the line of credit provided to the Central Bank of Venezuela under the Aladi Agreement, in the exercise of Article 27, paragraph two, of said Agreement.

27

Through Resolution 2096E-01-170927, the Board puts on record that banks will be understood to be authorized, in accordance with the provisions of Section 35, N° 3, of the Bank's Basic Constitutional Act and Chapter III.G.3 of the *Compendium of Financial Regulations*, to allow overdrafts on bank checking accounts in order to record the difference deriving the rounding up to the next ten pesos in the case of cash payments, due to the application of Article 13 of Law 20,956.

OCTOBER

5

Through Resolution 2099-01-171005, the Board appointed Mr. Rodrigo Alfaro Arancibia to replace Mr. Rodrigo Caputo Galarce as a full member of the National Commission on Price Distortions, described in Article 11 of Law 18,525.

5

Through Resolution 2099-02-171005, the Board approved the modification to Chapters III.F.4 and III.F.7 of the *Compendium of Financial Regulations,* on "Pension Fund Investment Limits" and "Financial Regulations Applicable to the Unemployment Fund Management Corporation, Established under Law 19,728 on Unemployment Insurance," respectively, in order to define the structural investment limits on alternative assets for the pension funds and the Solidarity Unemployment Fund (SUF), in accordance with the provisions of Article 45 of Decree Law 3500 of 1980 and Article 58 B of Law 19,728.

This regulation was previously opened for public comment through Resolution 2092-01-170914.

19

Through Resolution 2102-01-171019, the Board accepted the compensation owed to the Central Bank for its performance of fiscal agent duties in relation to the management of the resources held in the Economic and Social Stabilization Fund and the Pension Reserve Fund, for the period from 1 January to 31 December 2018.

19

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to hold the monetary policy interest rate at 2.5% in annual terms.

26

Through Resolution 2103-02-171026, the Board published for public comment the proposed new Chapter III.D.2 of the *Compendium of Financial Regulations,* entitled "Recognition and Regulation of Master Agreements for Derivative Contracts."

NOVEMBER

2

Through Resolution 2104-04-171102, the Board approved modifications to Part One of the *Compendium of Monetary and Financial Regulations* and the *Compendium of Financial Regulations,* in order to implement the second phase of the project to upgrade the technological platform used for the open market operations system. These modifications entered into effect on 27 November 2017.

2

Through Resolution 2104-05-171102, the Board approved modifications to the regulations on the issue and operation of payment cards, contained in Chapters III.J.1.1, III.J.1.3, and III.J.2, of the *Compendium of Financial Regulations,* including adjustments to the liquidity reserve requirements established therein.

9

Through Resolution 2106-01-171109, the Board accepted the Bank's compensation for fiscal agent duties performed in the issue and prepayment of public debt securities issued by the General Treasury in the local capital market, and the management thereof, to be performed in the period from 1 January to 31 December 2018, as is its due.

14

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to hold the monetary policy interest rate at 2.5% in annual terms.

23

Through Resolution 2110-01-171123, the Board modified its operating regulations to incorporate adjustments to the monetary policy meeting schedule, reducing the meeting frequency from 12 to 8 per year. This and other modifications will enter into effect on 1 January 2018.

23

Through Resolution 2110-02-171123, the Board modified the publication of the *Financial Stability Report*, which will now be published semiannually in May and November of each year. This Resolution will enter into effect on 1 January 2018.

23

Through Resolution 2110-04-171123, the Board modified the Bank's communication policy to reflect the changes in the monetary policy meeting schedule, which will enter into effect on 1 January 2018.

DECEMBER

14

At its monthly monetary policy meeting, the Board of the Central Bank of Chile voted to hold the monetary policy interest rate at 2.5% in annual terms.

15

The Board announced that the Bank has adopted extraordinary measures to facilitate the normal functioning of the foreign currency money market and interbank liquidity in foreign currency, which have tightened due to an increased use of currency hedging operations. The following measures were implemented starting on 18 December:

—A dollar swap program, with a 30-day maturity and up to US$500 million available during each auction. The Board further announced that there would be a total of eight auctions in the period.

—To complement the above program and offset its monetary effects, the Bank offered repo operations to inject liquidity in pesos, at the same maturity and in the same period as the dollar swap program.

21

Through Resolution 2117-05-171221, the Board opened a public consultation on the proposal to eliminate the daily calculation and publication of the reference exchange rate (*dólar acuerdo*) and the associated basket of currencies, with the modification of paragraph 7 of Chapter I of the *Compendium of Foreign Exchange Regulations* and its appendix, together with a corresponding adjustment to Resolution 1493-02-090806 on the statistics published by the Bank. The change is effective on 10 January 2018.

28

Through Resolution 2119E-01-171228, the Board approved the incorporation of a new Chapter III.H, on payment systems, in the *Compendium of Financial Regulations*, in relation to adherence to the Principles for Financial Market Infrastructures (PFMI).

This regulation expressly requires the application of the Principles for Financial Market Infrastructures, published by the Bank for International Settlements (BIS) and the International Organization of Securities Commissions (IOSCO) in 2012, in the large-value payment systems mentioned therein. This regulation was issued in accordance with the power conferred on the Bank by Section 35 N° 8 of the Bank's Basic Constitutional Act. It reflects the commitment assumed in January 2017 by several regulatory Chilean authorities, including the Central Bank, on the application of these principles in their policies, regulations, and supervisory and regulatory procedures, in accordance with the legal framework.

This regulation was previously opened for public consultation through Resolution 2116E-01-171215.

APPENDIX IV
INTERNATIONAL RESERVE MANAGEMENT

A. INTRODUCTION

International reserves are liquid foreign currency assets held by the Central Bank of Chile to support its monetary and foreign exchange policies. They are one of the instruments available to the Bank to meet its permanent objective of safeguarding the stability of the currency and the normal operation of the internal and external payment systems.

The management of these reserves aims to guarantee secure, efficient access to international liquidity and to safeguard the financial equity of the Bank. To achieve this, the Bank acts according to the legal framework stipulated in Section 38 of its Basic Constitutional Act, which specifically grants it the authority to manage, maintain, and use its international reserves abroad.

In line with the Bank's transparency policies[20]/, this appendix reports on the annual international reserve management. The next section describes the investment policies and benchmark structure used in managing reserves. The third section (C) reports on external portfolio managers. The fourth section (D) summarizes the risk management policies and the results of the international reserve management.

B. INVESTMENT POLICY AND BENCHMARK STRUCTURE

The international reserve investment policy is centered on liquid financial assets that meet the legal requirements established for reserve management. The policy is designed based on the impact on earnings and risk on the Central Bank's balance sheet and the characteristics of potential foreign exchange liquidity needs, oriented fundamentally toward the preservation of capital in the face of possible market fluctuations.

The management objectives of the investment policy are as follows: (i) to hold foreign exchange reserves in highly liquid instruments, which can be called in the briefest period possible without incurring in significant transaction costs, so as to be able to cover residual short-term external debt if necessary; (ii) to invest in instruments that present limited financial risks, in order to limit the risk of generating capital losses; (iii) to minimize the volatility of the value of the Bank's equity as a result of changes in the exchange rates of the investment currencies vis-à-vis the peso, with the goal of reducing any negative effects on the Bank's balance sheet; and (iv) to reduce the cost of holding reserves at the margin. This last objective led to the creation of a portfolio oriented toward achieving higher absolute returns in the long run.

Total international reserves are made up of the investment portfolio plus the cash portfolio (transaction account balances held by the General Treasury, public companies, and banks) and the other assets portfolio (IMF special drawing rights, or SDRs, certified gold, and other assets). The cash portfolio is allocated to covering expected funding requirements in the short term and is the preferred source for handling the daily funding requirements deriving from withdrawals from the foreign currency accounts maintained at the Central Bank by commercial banks and the public sector.

B.1 Benchmark structure of the investment portfolio

The benchmark structure of the investment portfolio establishes the basic parameters that guide the currency composition, duration, credit risk distribution, type of instrument, and the respective benchmarks used to measure performance.

The benchmark structure defines three investment portfolios: the short-term liquidity portfolio, the medium-term liquidity portfolio, and the diversification portfolio (table 1).

[20]/ Board Resolution 1289-01-060831.

TABLE 1

BENCHMARK STRUCTURE FOR THE INTERNALLY MANAGED INVESTMENT PORTFOLIO

		Tranche (years)	% of internally managed portfolio	% of sub-portfolio	Duration (months)	Benchmark indices
Short-term liquidity	USD	0-1	24.7	100.0	3.1	Merrill Lynch U.S. Treasury Bills (unhedged)
	Total		**24.7**	**100.0**	**3.1**	
Medium-term liquidity	USD	1-3	33.9	54.0	22.9	Global Aggregate - Treasury Bond Index (Unhedged) (EUR only Germany)
		3-5	3.8	6.0	45.8	
		Total	37.7	60.0	25.2	
	EUR	1-3	14.1	22.5	21.6	
		3-5	1.6	2.5	46.9	
		Total	15.7	25.0	24.1	
	CAD	1-3	4.2	6.8	21.9	
		3-5	0.5	0.8	45.5	
		Total	4.7	7.5	24.3	
	AUD	1-3	4.2	6.8	24.9	
		3-5	0.5	0.8	43.9	
		Total	4.7	7.5	26.8	
	Total		**62.7**	**100.0**	**25.0**	
Diversification (Internal)	USD	5-7	2.2	17.7	67.6	Global Aggregate - Treasury Bond Index (Unhedged) (EUR only Germany)
		7-10	0.3	2.4	92.0	
		Total	2.5	20.0	70.4	
	EUR	5-7	1.1	8.8	67.8	
		7-10	0.2	1.2	100.1	
		Total	1.3	10.0	71.6	
	CHF	5-7	0.6	4.4	64.0	
		7-10	0.1	0.6	95.6	
		Total	0.6	5.0	67.7	
	GBP	5-7	1.1	8.8	69.0	
		7-10	0.2	1.2	88.6	
		Total	1.3	10.0	71.3	
	JPY	5-7	0.3	2.7	68.9	
		7-10	0.0	0.4	98.1	
		Total	0.4	3.0	72.3	
	KRW	5-7	2.2	17.7	65.3	
		7-10	0.3	2.4	90.5	
		Total	2.5	20.0	68.2	
	NZD	5-7	1.3	10.6	56.1	
		7-10	0.2	1.4	87.9	
		Total	1.5	12.0	59.8	
	CNH	3 months	2.5	20.0	1.5	Bloomberg CGDRC Currency Index
	Total		**12.6**	**100.0**	**55.1**	
Total internally managed portfolio	**Total**		**100.0**		**23.4**	

Fuente: Central Bank of Chile.

The short-term liquidity portfolio represents 24% of the investment portfolio, and its currency structure is 100% U.S. dollars. The benchmark contemplates government bills issued by the United States, with a residual maturity of up to one year. The target duration is approximately three months. Investments can also be made in bills, bonds, discount notes, floating-rate notes, commercial papers, FIXBIS[21]/, and STRIPS[22]/, with a residual maturity of up to one year, from eligible issuers that represent sovereign, supranational, and agency risk. Investments are also allowed in deposits with a maturity of up to three months provided that they do no exceed 10% of portfolio. The short-term liquidity portfolio is designated, first and foremost, to be available for the potential use of foreign exchange reserves. In this portfolio, investments in currencies other than the U.S. dollar are not allowed.

The medium-term liquidity portfolio accounts for 61% of the investment portfolio, and its reference structure comprises 60% U.S. dollars, 25% euros, 7.5% Canadian dollars, and 7.5% Australian dollars. This benchmark includes sovereign securities issued by the United States, Germany, Canada, and Australia, with a residual maturity of one to five years. The target duration is approximately 25 months. Investments can be made in fixed- and floating-rate notes, nominal bonds, inflation-indexed bonds, MTIs,23 and STRIPS, with no restriction on residual maturity, from eligible issuers that represent sovereign, supranational, and agency risk. The main objective of the medium-term liquidity portfolio is to cover the Central Bank's balance sheet. This portfolio allows investments in currencies that are not included in the benchmark, provided they are hedged against one of the benchmark currencies.

The diversification portfolio represents 15% of the investment portfolio, and its benchmark structure comprises 20% U.S. dollars, 20% Chinese renminbi, 20% South Korean won, 12% New Zealand dollars, 10% euros, 10% pounds sterling, 5% Swiss francs, and 3% Japanese yen. With the exception of the renminbi, this benchmark includes sovereign securities issued by the United States, South Korea, New Zealand, Germany, the United Kingdom, Switzerland, and Japan, with a residual maturity of five to ten years. In the case of the renminbi, the benchmark is associated with the deposit rate on three-month bank deposits denominated in Chinese renminbi and traded offshore. The target duration of the portfolio is approximately 55 months. Investments can also be made in any and all instruments approved under the most recent *Current Policy Manual* for the *Management of Foreign Exchange Reserves*, with no restrictions on terms (or residual maturity) or currencies. The diversification portfolio is managed on the basis of a risk budget. Deviations from the benchmark are limited to an average monthly ex ante tracking error of 100 basis points (bp) per year,24 which cannot exceed 150 bp at any given time. The main objective of holding these assets is to increase returns at the margin so as to reduce the existing gap between the cost of the Bank's liabilities and the returns on its investments.

The investment portfolio has mechanisms for rebalancing the sub-portfolios to ensure that their relative size remains in line with the benchmark.

B.2 Benchmark Structure of the Cash Portfolio

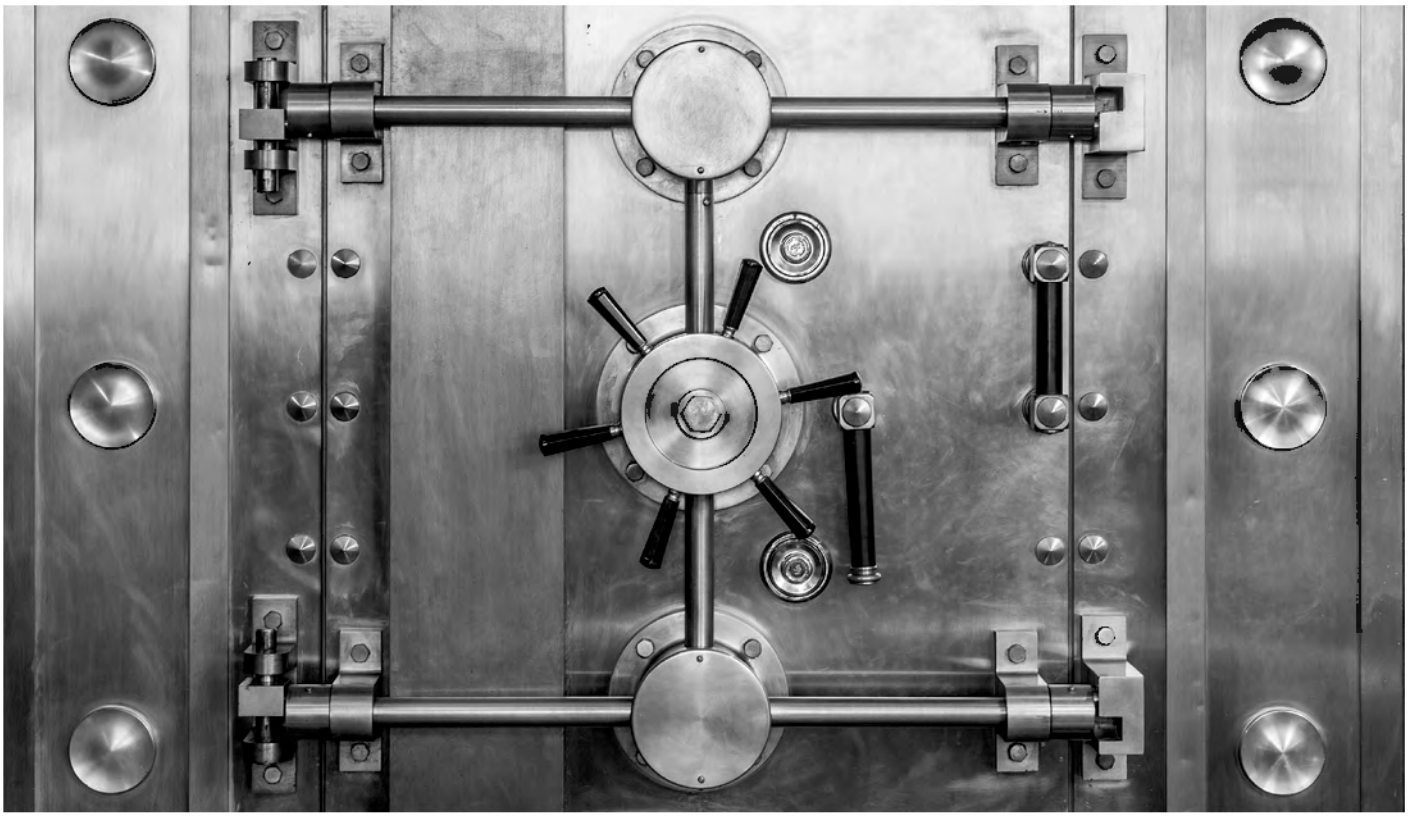
The investments in the cash portfolio match the currency and term structure of expected disbursements on the Bank's balance sheet. The currency composition of the cash portfolio is thus tied to the currency composition of expected disbursements and deposits and withdrawals in accounts held at the Central Bank by commercial banks and the public sector. The benchmark is calculated on the basis of the overnight, weekend, and time deposit rates of the reference currencies, as a function of the characteristics of expected disbursements.

B.3 Portfolio Performance in 2017

As of 31 December 2017, the investment portfolio stood at US$35.0710 billion, while the cash portfolio held US$2.8770 billion. Taking the sum of these two portfolios plus other assets[25]/, total international reserves closed the year at US$38.9826 billion. This balance was US$1.5110 billion lower than at year-end 2016. The decrease is explained by a reduction in the cash portfolio of US$3.0795 billion, which was partially offset by an increase of US$66.6 million in the other assets portfolio and US$1.5019 billion in the investment portfolio. The increase in the investment portfolio is mainly explained by the appreciation of the investment currencies against the U.S. dollar, while the increase in the other assets portfolio derives from transactions with the IMF. In the case of the cash portfolio, the contraction

[21]/ Fixed-Rate Investment at the BIS: Short-term fixed-income securities issued by the Bank for International Settlements.
[22]/ Separate Trading of Registered Interest and Principal Securities: Cero-coupon securities backed by U.S. Treasury notes and bonds.
[23]/ Medium-Term Instruments: Medium-term fixed-income securities issued by the Bank for International Settlements (BIS).

[24]/ The tracking error identifies the incremental risk incurred by a portfolio, relative to the benchmark, when it takes positions outside the benchmark. For the purposes of management, limits can be imposed on this incremental risk, and these limits are known as a risk budget.
[25]/ The other assets portfolio is mainly composed of monetary gold and IMF special drawing rights (SDRs).



is due to a decrease in the foreign currency deposits held by local banks at the Central Bank. In addition, there was a withdrawal of US$30 million from the investment portfolio in December, for the dollar swap program implemented by the Central Bank.

With regard to the value of the investment portfolio, US$8.3144 billion was in the short-term liquidity portfolio, US$21.2849 billion was in the medium-term liquidity portfolio, US$5.3196 billion was in diversification portfolio, and US$46.0 was in current accounts. At year-end, there were also investments in onshore Chinese government bonds, through investments in a BIS Investment Pool denominated in renminbi (BISIP CNY), for a total of US$106.1 million. In addition, at year-end a share of the diversification portfolio was managed by two external managers, as described in section C of this appendix.

Of the US$33.9113 billion in the internally managed portfolio[26]/, 94.0% was invested in sovereign risk, 3.0% in supranational risk[27]/, 0.7% in agency risk[28]/, and 2.3% in bank risk. Relative to year-end 2016, there was an increase in exposure to sovereign risk and a decrease in exposure to bank and supranational risk.

Sovereign risk includes investments in the United States (56.2%), Germany (20.8%), Canada (5.3%), Australia (4.4%), South Korea (2.6%), Poland (1.7%), Japan and New Zealand (1.5% each), Ireland (1.2%), Austria (1.1%), Italy (0.9%), Spain (0.8%), United Kingdom and Switzerland (0.6% each), Finland and France (0.3% each), and China (0.2%). Supranational risk is made up entirely of issues by the European Investment Bank (74.9%), the Inter-American Development Bank (8%), the International Bank for Reconstruction and Development (6.2%), the European Company for the Financing of Railroad Rolling Stock (EUROFIMA) (6.2%), the Asian Development Bank (2.8%), the European Bank for Reconstruction and Development (1%), and the Bank for International Settlements (1%). Agency risk is concentrated in one issue from Landwirtschaftliche Rentenbank (Germany). Finally, bank risk comprises deposits denominated in U.S. dollars and Chinese renminbi, in banks Germany, France, Sweden, and Singapore.

At year-end 2017, the cash portfolio stood at US$2.8770 billion.

The currency composition of total reserves and the investment portfolio is given in tables 2a and 2b.

[26]/ The investment portfolio excluding the BIS investment pool shares and the externally managed resources.
[27]/ Supranational institutions are multilateral financial institutions, whose articles of agreement are signed by the governments of two or more countries.
[28]/ Agencies are financial institutions with specific objectives; they are fully or partially backed by the government of the country in which they are established.

TABLE 2A

COMPOSITION OF INTERNATIONAL RESERVES

(millions of dollars)

Portfolio	Currency	2016		2017	
		Dec	%	Dec.	%
Investment portfolio		**33,569.1**	**82.9**	**35,071.0**	**90.0**
Currencies and deposits	USD	771.7	1.9	23.3	0.1
	EUR	4.0	0.0	0.3	0.0
	CAD	26.6	0.1	0.2	0.0
	AUD	1.2	0.0	1.2	0.0
	Other	683.4	1.7	810.7	2.1
Securities	USD	20,914.1	51.6	22,260.3	57.1
	EUR	5,484.5	13.5	5,832.8	15.0
	CAD	1,536.3	3.8	1,662.1	4.3
	AUD	1,498.1	3.7	1,679.9	4.3
	Other	2,649.3	6.5	2,800.2	7.2
Total	USD	21,685.7	53.6	22,283.6	57.2
	EUR	5,488.5	13.6	5,833.2	15.0
	CAD	1,562.9	3.9	1,662.2	4.3
	AUD	1,499.3	3.7	1,681.0	4.3
	Other	3,332.6	8.2	3,610.9	9.3
Cash portfolio		**5,956.5**	**14.7**	**2,877.0**	**7.4**
Currencies and deposits	USD	5,956.5	14.7	2,877.0	7.4
Other assets portfolio		**968.0**	**2.4**	**1,034.6**	**2.7**
Monetary gold	Other	9.1	0.0	10.2	0.0
IMF SDRs	Other	727.2	1.8	770.3	2.0
IMF reserve position	Other	215.3	0.5	251.1	0.6
Reciprocal credit agreements	USD	15.0	0.0	2.1	0.0
Currencies and deposits	USD	1.4	0.0	0.9	0.0
Total international reserves		**40,493.6**	**100.0**	**38,982.6**	**100.0**
	USD	27,658.6	68.3	25,163.6	64.6
	EUR	5,488.5	13.6	5,833.2	15.0
	CAD	1,562.9	3.9	1,662.2	4.3
	AUD	1,499.3	3.7	1,681.0	4.3
	Other	4,284.3	10.6	4,642.6	11.9

Source: Central Bank of Chile.

TABLE 2B

INVESTMENT PORTFOLIO, BY CURRENCY

(percent, as of 31 December 2017)

Currency	Share (1)
U.S. dollar	63.3
Euro	16.6
Canadian dollar	4.7
Australian dollar	4.7
South Korean won	2.9
Chinese renminbi	3.3
New Zealand dollar	1.9
Pound sterling	1.3
Swiss franc	0.7
Japanese yen	0.3
Other (2)	0.4
Total	**100.0**

(1) Including currency forwards.
(2) Other currencies: Czech koruna, Danish krone, Norwegian krone, Swedish krona, Singapore dollar, and Malaysian ringgit.

Source: Central Bank of Chile.

C. EXTERNAL PORTFOLIO MANAGEMENT PROGRAM

At year-end 2017, a portion of the investment portfolio was managed by two external managers: BlackRock Institutional Trust Company N.A. and Amundi Asset Management. The firms were brought on in February and October 2016, respectively, with a mandate of US$500 million each. Both firms manage a long-term global government fixed-income mandate, with a structure equivalent to the internally managed diversification portfolio.

The external portfolio managers also manage a share of the diversification portfolio, based on the same guidelines and risk budget defined for the internally managed diversification portfolio.

The priority objectives of the external management program are twofold: (i) to provide an active benchmark for the internally managed diversification portfolio; and (ii) to add value to the international reserve portfolio.

D. RISK MANAGEMENT AND RETURNS FROM INTERNATIONAL RESERVE MANAGEMENT

D.1 Risk Management in International Reserve Management

International reserve management includes criteria for limiting liquidity, credit, market, and operational risks.

To reduce liquidity risk, the Bank manages a portfolio composed mainly of fixed-income instruments traded in deep and highly liquid secondary markets. Investments in bank deposits are limited to the instruments defined for the cash portfolio (primarily overnight deposits) and the short-term liquidity portfolio.

With regard to credit risk, limits are applied to bank, sovereign, supranational, and agency (external financial institution) risk, as well as to the counterparties used (table 3).

TABLE 3

COMPOSITION OF INTERNATIONAL RESERVES BY CREDIT RISK (1)(2)(3)(4)

(percent, as of 31 December 2017)

Type of risk	Credit rating									
	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	Total
Agency	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.7
Bank	0.0	0.0	0.5	3.9	1.9	3.4	0.0	0.0	0.0	9.7
Sovereign	74.2	1.3	5.3	0.0	3.0	0.0	1.4	0.6	0.8	86.7
Supranational	2.7	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	2.9
Total	**77.6**	**1.5**	**5.8**	**3.9**	**4.8**	**3.4**	**1.4**	**0.6**	**0.8**	**100.0**

(1) Bank risk is related to investment in banks' financial instruments (deposits). Sovereign risk is related to investment in instruments from sovereign states (bills, nominal bonds); it includes investments in a BIS Investment Pool denominated in CNY, associated with Chinese sovereign risk. Agency risk is associated with investment in instruments from German government agencies (bills, nominal bonds). Supranational risk is associated with investment in instruments from an official multilateral issuer (deposits, bills, and nominal bonds).
(2) For sovereign risk, the credit rating corresponds to the average rating from Fitch, Moody's, Standard and Poor's, and Dominion Bond Rating Service.
(3) For agency, bank, and supranational risk, the credit rating corresponds to the average rating from Fitch, Moody's and Standard and Poor's.
(4) Including the cash portfolio; excluding the other assets portfolios.

Source: Central Bank of Chile.

The investment guidelines establish other criteria and restrictions as complementary measures to limit credit risk, including eligibility criteria for issuers, operations, and intermediaries and rules on the treatment of derivatives (tables 4, 5, and 6).

Financial institutions with outstanding deposits as of 31.Dec.2017 (1) (2)	
AAA, AA, AA-	DZ BANK AG Deutsche Zentral-Genossenschaftsbank J.P. Morgan Chase Bank Oversea-Chinese Banking Corp Ltd. Svenska Handelsbanken AB (publ) Wells Fargo Bank, NA Minimum 46 Maximum 650 Category average 328
A+, A, A-	China Construction Bank Corporation Citibank, NA Danske Bank Aktieselskab DekaBank Deutsche Girozentrale Société Générale Sumitomo Mitsui Banking Corporation Minimum 180 Maximum 499 Category average 338

(1) Includes the internally managed investment portfolio and the cash portfolio.
(2) Includes balances held in remunerated current accounts.

Source: Central Bank of Chile.

TABLE 5

ELIGIBLE BANKS AND PERMISSIBLE LIMITS AS OF 31 DECEMBER 2017

(US$ million and months)

Country	Bank	Amount	Duration
Germany	Bayerische Landesbank	150	1
Germany	DekaBank Deutsche Girozentrale	500	3
Germany	Deutsche Bank AG	150	1
Germany	DZ BANK AG Deutsche Zentral-Genossenschaftsbank	700	9
Germany	Landesbank Baden-Wurttemberg	150	1
Germany	Landesbank Hessen-Thüringen Girozentrale	500	3
Germany	NRW.BANK	700	9
Australia	Australia & New Zealand Banking Group Limited	700	9
Australia	Commonwealth Bank of Australia	700	9
Australia	National Australia Bank Ltd	700	9
Australia	Westpac Banking Corporation	700	9
Belgium	Belfius Bank SA/NV	150	1
Belgium	BNP Paribas Fortis SA/NV	500	3
Belgium	ING Belgium SA/NV	500	3
Belgium	KBC Bank NV	500	3
Canada	Bank of Montreal	500	3
Canada	Canadian Imperial Bank of Commerce	500	3
Canada	National Bank of Canada	500	3
Canada	Royal Bank of Canada	700	9
Canada	The Bank of Nova Scotia	500	3
Canada	The Toronto-Dominion Bank	700	9
China	Bank of China (Hong Kong) Ltd.	500	3
China	China Construction Bank Corporation	500	3
China	Industrial and Commercial Bank of China (Asia) Ltd	500	3
China	Industrial and Commercial Bank of China Ltd	500	3
China	The Hongkong and Shanghai Banking Corporation Limited	700	9
South Korea	Standard Chartered Bank Korea Limited	500	3
Denmark	Danske Bank A/S	500	3
Denmark	Nykredit Bank A/S	250	3
Spain	Banco Bilbao Vizcaya Argentaria S.A.	150	1
Spain	Banco Santander S.A.	150	1
France	Bred Banque Populaire	250	3
France	Credit Agricole Corporate and Investment Bank	500	3
France	Credit Agricole S.A.	500	3
France	Crédit Industriel et Commercial (CIC)	500	3
France	HSBC France	700	9
France	Société Générale	500	3
France	BNP Paribas SA	500	3
France	Natixis SA	500	3
Netherlands	ABN AMRO Bank NV	500	3
Netherlands	ING Bank NV	500	3

TABLE 5

ELIGIBLE BANKS AND PERMISSIBLE LIMITS AS OF 31 DECEMBER 2017

(US$ million and months)

continued

Country	Bank	Amount	Duration
Netherlands	NV Bank Nederlandse Gemeenten	1000	12
Netherlands	Coöperatieve Rabobank UA	700	9
Israel	Bank Hapoalim B.M.	500	3
Japan	Mizuho Bank, Ltd.	500	3
Japan	Sumitomo Mitsui Banking Corporation	500	3
Japan	Sumitomo Mitsui Trust Bank Ltd.	500	3
Japan	The Bank of Tokyo-Mitsubishi UFJ, Ltd.	500	3
Japan	The Chiba Bank, Ltd.	500	3
Japan	The Norinchukin Bank	500	3
Japan	The Shizuoka Bank Ltd.	500	3
Norway	DNB Bank ASA	500	3
Poland	Bank Polska Kasa Opieki SA (Bank Pekao SA)	150	1
Singapore	DBS Bank Ltd	700	9
Singapore	Oversea-Chinese Banking Corp Ltd.	700	9
Singapore	United Overseas Bank Limited	700	9
Sweden	Nordea Bank AB	700	9
Sweden	Skandinaviska Enskilda Banken AB (Publ) (SEB)	700	9
Sweden	Svenska Handelsbanken AB (publ)	700	9
Sweden	Swedbank AB	700	9
Switzerland	Credit Suisse AG	500	3
Switzerland	UBS AG	700	9
Switzerland	Zürcher Kantonalbank	1000	12
United Kingdom	Bank of Scotland Plc	500	3
United Kingdom	Bank Plc	500	3
United Kingdom	Goldman Sachs International Bank	250	3
United Kingdom	HSBC Bank Plc	700	9
United Kingdom	Lloyds Bank Plc	500	3
United Kingdom	Merrill Lynch International	500	3
United Kingdom	Santander UK PLC	500	3
United Kingdom	Standard Chartered Bank	500	3
United Kingdom	UBS Limited	250	3
United States	Bank of America NA	500	3
United States	BNY Mellon National Association	500	9
United States	Citibank, NA	500	3
United States	Comerica Bank	500	3
United States	Deutsche Bank Trust Company Americas	150	1
United States	Goldman Sachs Bank USA	500	3
United States	HSBC Bank USA N.A.	700	9
United States	JPMorgan Chase Bank N.A.	700	9
United States	Keybank National Association	150	1
United States	PNC Bank NA	500	3
United States	State Street Bank & Trust Company	700	9
United States	The Bank of New York Mellon	700	9
United States	The Northern Trust Company	700	9
United States	U.S. Bank N.A.	700	9
United States	Wells Fargo Bank, NA	700	9

Source: Central Bank of Chile.

TABLE 6

INTERMEDIARIES USED IN 2017

Intermediaries
ABN Amro Bank N.V.
ANZ Securities Inc.
Australia & New Zealand Banking Group Limited
Banco Bilbao Vizcaya Argentaria SA
BIS
Bank of China Limited
Bank of Nova Scotia, New York Agency
Barclays Bank PLC
Barclays Capital Inc.
BMO Capital Markets Corp.
BNP Paribas
BNP Paribas Securities Corp.
Bred Banque Populaire
CIBC World Markets Corp.
Citigroup Global Markets Inc.
Citigroup Global Markets Limited
Commerzbank
Commonwealth Bank of Australia
Credit Agricole Corporate and Investment Bank
Credit Suisse
Credit Suisse Securities (USA) LLC
Daiwa Capital Markets America Inc.
Danske Markets Inc.
Deutsche Bank AG
Deutsche Bank Securities Inc.
DZ Bank AG Deutsche Zentral Genossenschaftsbank
Goldman Sachs International Bank
Goldman, Sachs & Co. LLC
HSBC Bank (China) Co., Ltd.
HSBC Bank PLC
HSBC Securities (USA) Inc.
ING Bank NV
JP Morgan Securities LLC
Jefferies International LTD.
Jefferies LLC
JP Morgan Securities PLC
JPMorgan Chase Bank, N.A.
Landesbank Baden-Wurttemberg
Lloyds Bank PLC
Merrill Lynch International
Merrill Lynch, Pierce, Fenner & Smith Incorporated
Mizuho Securities USA Inc.
Mizuho Securities USA LLC
Morgan Stanley & Co. International plc

TABLE 6
INTERMEDIARIES USED IN 2017
continued

Intermediaries
Morgan Stanley & Co. LLC.
MUFG Securities Americas Inc.
National Australia Bank Ltd
National Bank of Canada Financial Inc.
Natixis
Nomura International Plc
Nomura Securities International, Inc.
Nordea Bank AB
Nordea Bank Finland Plc
RBC Capital Markets, LLC
RBS Securities Inc
Scotia Capital (USA) Inc
Shangai Pudong Development Bank Co., Ltd. (Only China Mainland)
Skandinaviska Enskilda Banken AB
Société Générale
Standard Chartered Bank (China) Co., Ltd.
Standard Chartered Securities Korea Limited
TD Securities (USA) LLC.
The Royal Bank of Scotland Plc
UBS AG
UBS Limited
UBS Securities LLC, USA
Wells Fargo Securities, LLC
Westpac Banking Corporation
Zurcher Kantonalbank

Source: Central Bank of Chile.

Market risk is contained through the diversification of investment currencies, instruments, and maturities and through the measurement and control of limits on exposure to duration and currency risk described above.

The average daily value at risk (VaR29) of the internally managed investment portfolio was 1.58% in 2017 (2.43% in 2016). The average tracking error 11 basis points.

Operational risk is controlled through the separation of functions and responsibilities at the institutional and hierarchical levels, the application of efficient controls to mitigate it, and the use of computer applications that adhere to market quality standards. Initiatives were carried out to improve the standards of operational continuity, and a contingency unit was maintained to guarantee the operational continuity of both the international reserves and the fiscal resources in the event of problems with the physical or technological infrastructure of the Central Bank building.

D.2 Return on International Reserve Management

In 2017, the total return on reserve management was 0.77% measured in the currency of origin of the investments. Measured in U.S. dollars, the return was 4.17%. The return in local currency was complemented by the positive exchange rate effect deriving from measuring the reserve returns in U.S. dollars. The return differential relative to the benchmark structure was 10.8 bp. For the 2008-2017, period, reserve management recorded an average return differential of 5.8 bp (table 7).

[29]/ The VaR is based on a parametric model with an annualized daily horizon, a confidence level of 84% (one standard deviation), and a decay factor of 0.94.

TABLE 7

ABSOLUTE RETURNS ON INTERNATIONAL RESERVES AND THE BENCHMARK (1) (2)

(percent)

Period	In currency of origin			In U.S. dollars		
	Int. Res.	Benchmark	Differential	Int. Res.	Benchmark	Differential
2017	0.77	0.62	0.15	4.17	4.06	0.11
2016	0.90	0.90	0.00	0.13	0.17	-0.04
2015	0.73	0.90	-0.17	-3.74	-3.58	-0.16
2014	1.65	1.52	0.13	-2.94	-3.14	0.21
2013	0.26	0.21	0.06	-0.71	-0.77	0.06
2012	0.66	1.01	-0.35	1.43	1.77	-0.35
2011	2.43	2.41	0.02	1.22	1.20	0.02
2010	2.10	2.19	-0.09	-0.15	-0.06	-0.09
2009	2.15	1.65	0.50	3.34	2.85	0.50
2008	5.70	5.37	0.33	4.14	3.81	0.33
Average	**1.74**	**1.68**	**0.06**	**0.69**	**0.63**	**0.06**

(1) Excludes holdings of monetary gold, special drawing rights, IMF reserve position, reciprocal credit agreements, and other reserve assets.
(2) Starting in 2014, the return is measured in currency of origin, which does not incorporate appreciations or depreciations of the currencies in the portfolio. In contrast, from 2007 to 2013, the return in currency of origin was approximated using a foreign exchange measure based on the basket of currencies in the benchmark, which is equivalent to the return in currency of origin for investments that replicate the benchmark.

Source: Central Bank of Chile.

D.3 Securities Lending Program

In the period, a securities lending program was maintained with the Bank's international reserve custodians. This consists in lending instruments owned by the Bank to primary dealers, who must put up collateral equivalent to 102 or 105% of the value of the instrument being loaned, as contractually required. Primary dealers are financial institutions designated by the treasury offices of the issuing countries, for the placement and distribution of their debt securities. The contractual relationship with the lending agent—that is, the custodian—incorporates a clause stipulating that in the event of default by the debtor, the custodian will be responsible for the totality of the positions loaned, thereby transferring the risk from the debtor to the custodian bank. In addition, the custodian keeps the custodial positions in separate accounts on its balance sheet, so there is no credit risk. In 2017, this program generated income for the Bank equivalent to 0.9 bp of total foreign exchange reserves.

APPENDIX V
MANAGEMENT OF FISCAL FUNDS (ESSF AND PRF)

A. INTRODUCTION

As fiscal agent, the Central Bank of Chile manages resources in the name and on the account of the General Treasury. These resources are part of the Economic and Social Stabilization Fund (ESSF) and the Pension Reserve Fund (PRF).

The following sections describe the institutional context in which this fiscal agency operates. They also report on the investment policy, the fund structure, the reporting system, the management results, and the costs of managing the resources.

B. INSTITUTIONAL FRAMEWORK

In September 2006, Law 20,128 on Fiscal Responsibility created the ESSF and the PRF. Under this law, the Ministry of Finance issued Executive Decree 1383 (which was modified by Decree 1618), whereby the Central Bank is vested with the representation of the General Treasury for investing all or part of the ESSF and PRF resources, once the Bank has formally accepted the fiscal agency agreement in accordance with its Basic Constitutional Act.

C. INVESTMENT POLICY AND OBJECTIVES

The investment policy objectives for the fiscal portfolios and the associated risk-return profile reflect decisions made by the Ministry of Finance. The Central Bank must manage the fiscal resources in accordance with the relevant decrees and performance guidelines.

The performance guidelines contain the investment criteria, which define a benchmark and place restrictions on fiscal portfolio management. The benchmark structure implicitly incorporates risk-return objectives established by the Ministry of Finance. The fiscal agent's performance is assessed against these benchmark portfolios.

For the ESSF, managed internally by the Central Bank of Chile, the benchmark portfolio established in the performance guidelines is made up of the following asset classes: bank assets[30]/; treasury bills and sovereign bonds; and inflation-indexed sovereign bonds (table 1). The bank asset and treasury bill portfolios use benchmark indices provided by Merrill Lynch. The sovereign bond share of the portfolio and the inflation-indexed sovereign bond portfolio are compared against selected currency indices provided by Barclays Capital.

TABLE 1
BENCHMARK FOR THE ESSF PORTFOLIO MANAGED BY THE CENTRAL BANK
(percent)

Asset class	Share
Bank assets	16.2
Treasury bills and sovereign bonds	80.0
Inflation-indexed sovereign bonds	3.8

Source: Ministry of Finance.

For the PRF portfolio that is directly managed by the fiscal agent, the current investment policy establishes a portfolio composition made up of the following asset classes: sovereign bonds and related assets; and inflation-indexed sovereign bonds (table 2). The benchmarks for these assets are global indices provided by Barclays Capital.

[30]/ Bank deposits.

TABLE 2

BENCHMARK FOR THE PRF PORTFOLIO MANAGED BY THE CENTRAL BANK

(percent)

Asset class	Share
Sovereign bonds and related assets	73.8
Inflation-indexed sovereign bonds	26.2

Source: Ministry of Finance.

The ESSF and PRF investment guidelines define eligible currencies, issuers, and instruments as those included in the respective benchmarks, and they exclude any and all instruments from Chilean issuers or denominated in pesos.

Under the current guidelines, the management mandate controls the main portfolio risks through risk budgets. The internally managed ESSF and PRF portfolios establish an ex ante tracking error of 50 basis points (bp) per year.

Finally, the investment guidelines for both funds establish specific rules and limits on exposure, including eligibility criteria for issuers, operations, instruments, and intermediaries and rules on the treatment of derivatives (tables 4 and 5).

D. STRUCTURE OF FISCAL PORTFOLIOS

At year-end 2017, the market value of the ESSF and PRF portfolios managed directly by the Fiscal Agent was US$13.5369 billion and US$6.4243 billion[31]/ respectively, which is invested in line with the benchmark composition established in the current investment guidelines (table 3).

TABLE 3

PORTFOLIOS MANAGED BY THE CENTRAL BANK

(as of 31 December 2017; US$ million)

Portfolio / Asset class	Market value (1)						Share of total
	USD	EUR	JPY	CHF	Other (2)	Total	
ESSF							
Bank assets / Treasury bills and sovereign bonds	5,480.7	3,515.4	2,924.4	1,101.8	n/a	13,022.3	96.2
Inflation-indexed sovereign bonds	366.6	148.0	n/a	n/a	n/a	514.6	3.8
Total	**5,847.3**	**3,663.4**	**2,924.4**	**1,101.8**	**n/a**	**13,536.9**	**100.0**
PRF							
Sovereign bonds and related assets	1,394.0	1,313.8	1,180.4	16.7	790.1	4,695.1	73.1
Inflation-indexed sovereign bonds	688.6	400.2	7.2	0.0	633.1	1,729.2	26.9
Total	**2,082.6**	**1,714.0**	**1,187.6**	**16.7**	**1,423.3**	**6,424.3**	**100.0**

Portfolio	*Ex ante tracking error (bp)*	Risk budget (bp)
ESSF	2.8	50.0
PRF	13.0	50.0

n/a: Not available.
(1) These positions include currency forwards.
(2) Includes the Canadian dollar, Australian dollar, pound sterling, and other currencies.

Source: J.P. Morgan N.A.

[31]/ The market value of the ESSF on 31 December 2017 was US$14.7388 billion, of which US$13.5369 billion was managed internally by the Bank and US$1.2019 billion was managed by external portfolio managers under an equity mandate. The market value of the PRF at year-end 2017 was US$10.0110 billion, of which US$6.4243 billion was managed internally by the Bank and US$3.5867 was managed by external portfolio managers under equity and corporate bond mandates.

E. REPORTS

The Fiscal Agency Decree and the performance guidelines define the content and frequency of the reports that the Bank must deliver to the Finance Minister and the General Treasurer of Chile. As a general rule, the custodian bank, in its middle office role, provides the necessary information for preparing reports, and the fiscal agent must report daily, monthly, quarterly, and annually on the status of the resources under management. The daily reports provide information on the market value of each portfolio, under items sorted by currency and asset class. The monthly, quarterly, and annual reports contain more detailed information on the portfolios. These reports describe changes in financial markets, discuss compliance with investment caps, provide details on the changes in the market value of each fund, and report on the absolute and differential returns obtained.

The Central Bank also measures the custodian bank's performance and compliance with the investment guidelines, and monitors and assesses the information provided by the custodian. To this end, it uses its own calculation methods based on systematically recorded information.

The Fiscal Agent must report annually to the Finance Minister and the General Treasurer on the custodian bank's performance.

F. MANAGEMENT RESULTS

In 2017, the ESSF resources managed internally by the Bank generated an absolute return measured in dollars of 5.60%, which implies a positive differential return of 5.9 bp, relative to the benchmark performance, where both returns are calculated using the time-weighted rate of return (TWRR). Using the same methodology, the PRF resources managed by the Bank generated an absolute return measured in U.S.dollars of 7.97%, which implies a positive differential return of 4.5 bp relative to the benchmark performance. The appreciation of the investment currencies against the U.S. dollar had a significant effect on the absolute return of both portfolios.

G. COMPENSATION OF THE FISCAL AGENT

According to the stipulations of Article 9, letter (a), of the Fiscal Agency Decree, the Central Bank is entitled to charge an annual fee for the direct expenses and costs incurred in carrying out its assigned functions.

For the period from 1 January to 31 December 2017, the Ministry of Finance set the annual fee at US$932,360 for the ESSF and US$995,777 for the PRF[32]/. These amounts are consistent with the Central Bank's Basic Constitutional Act, which stipulates that the Bank shall not finance the General Treasury. The fees paid to the Fiscal Agent represent 0.7 and 1.6 bp of the total resources managed by the Bank for the ESSF and PRF, respectively.

TABLE 4

FINANCIAL INSTITUTIONS WITH OUTSTANDING DEPOSITS

(As of 31 December 2017)

Institution
ABN AMRO Bank N.V.
Banco Bilbao Vizcaya Argentaria S.A.
Banco Santander S.A.
Bank Hapoalim B.M.
Bank of China (Hong Kong), Ltd.
Bayerische Landesbank
BNP Paribas
Bred Banque Populaire
China Construction Bank Corporation
Coöperatieve Rabobank UA
Credit Agricole Corporate and Investment Bank
DekaBank Deutsche Girozentrale
HSBC France
Landesbank Baden-Württemberg
Mizuho Bank, Ltd.
Natixis
Nykredit Bank A/S
Société Générale
Standard Chartered Bank
Sumitomo Mitsui Banking Corporation
Sumitomo Mitsui Trust Bank, Ltd.
The Chiba Bank, Ltd.
The Shizuoka Bank, Ltd.

Source: J.P. Morgan N.A.

[32]/ The Fiscal Agency fees do not include payments to the external portfolio managers for the management of their respective portfolios.

TABLE 5

INTERMEDIARIES USED BY THE FISCAL AGENT IN 2017

Institution
ABN Amro Bank N.V., Amsterdam
ANZ Securities Inc., New York
Australia & New Zealand Banking Group Limited, Melbourne
Banco Bilbao Vizcaya Argentaria S.A., Madrid
Banco Santander S.A., Madrid
Bank Hapoalim B.M., New York Branch
Bank of China Limited, Hong Kong
Bank of Nova Scotia, Canada
Bank of Nova Scotia, New York Agency
Barclays Bank Plc.
Barclays Capital Inc.
Bayerische Landesbank, Muenchen
BMO Capital Markets Corp.
BNP Paribas (Head Office)
BNP Paribas Securities Corp., New York
BNP Paribas U.S.A., New York
BNP Paribas, London
Bred Banque Populaire, Paris
Caisse Centrale Desjardins, Montreal
Canadian Imperial Bank of Commerce, Toronto
China Construction Bank Corporation, London
CIBC World Markets Corp.
Citibank N.A., New York
Citigroup Global Markets Inc., New York
Citigroup Global Markets Limited, London
Commonwealth Bank of Australia, New York
Commonwealth Bank of Australia, Sydney
Credit Agricole Corporate And Investment Bank (Calyon New York)
Credit Suisse (Head Office), Zurich
Credit Suisse, New York Branch
Credit Suisse Securities (U.S.A) Llc., New York
Daiwa Capital Markets America Inc.
Danske Bank A/S, Copenhagen.
Danske Markets Inc.
Dbs Bank Ltd., London
Dekabank Deutsche Girozentrale, Frankfurt
Deutsche Bank A.G., London
Deutsche Bank A.G., New York
Deutsche Bank Securities Inc.
DZ Bank Ag Deutsche Zentral Genossenschaftsbank, Frankfurt
Goldman Sachs International Bank, London

continued

Institution
Goldman, Sachs & Co., New York
HSBC Bank Plc (All U.K. Offices), London
HSBC Bank U.S.A. N.A., New York.
HSBC France, Paris
HSBC Securities U.S.A Inc., New York
ING Bank N.V., Amsterdam
ING Bank N.V., Seoul
J.P. Morgan Chase Bank N.A., New York
J.P. Morgan Securities Llc., New York
Jefferies International Ltd., London
Jefferies Llc.
JP Morgan Chase Bank, N.A., London
JP Morgan Chase Bank, N.A., Seoul
JP Morgan Securities Plc.
Landesbank Baden Wurttemberg, Stuttgart
Lloyds Bank Plc., London
Merrill Lynch International
Merrill Lynch, Pierce, Fenner & Smith Incorporated
Mizuho Bank Ltd., New York
Mizuho Securities USA Inc.
Morgan Stanley & Co. International Plc., London
Morgan Stanley & Co. Llc.
MUFG Securities Americas Inc.
National Australia Bank Ltd., London
National Australia Bank Ltd., Melbourne
National Bank of Canada Financial Inc., New York
National Bank of Canada, Montreal
Natixis (Capital Markets), Paris
Natixis (Formerly Natexis Banque), New York
Nomura International Plc., London
Nomura Securities International Inc., New York
Nomura Securities International Inc., New York
Norddeutsche Landesbank Girozentrale, Hannover
Nordea Bank AB (Publ), Stockholm
Nykredit Bank A/S, Copenhagen
Rabobank Nederland, Utrecht
Rbc Capital Markets Llc.
Rbs Securities Inc., Greenwich
Royal Bank Of Canada, Toronto
Scotia Capital (USA) Inc.
Skandinaviska Enskilda Banken Ab, New York
Societe Generale, New York
Societe Generale, Paris
Standard Chartered Bank, New York

TABLE 5

INTERMEDIARIES USED BY THE FISCAL AGENT IN 2017

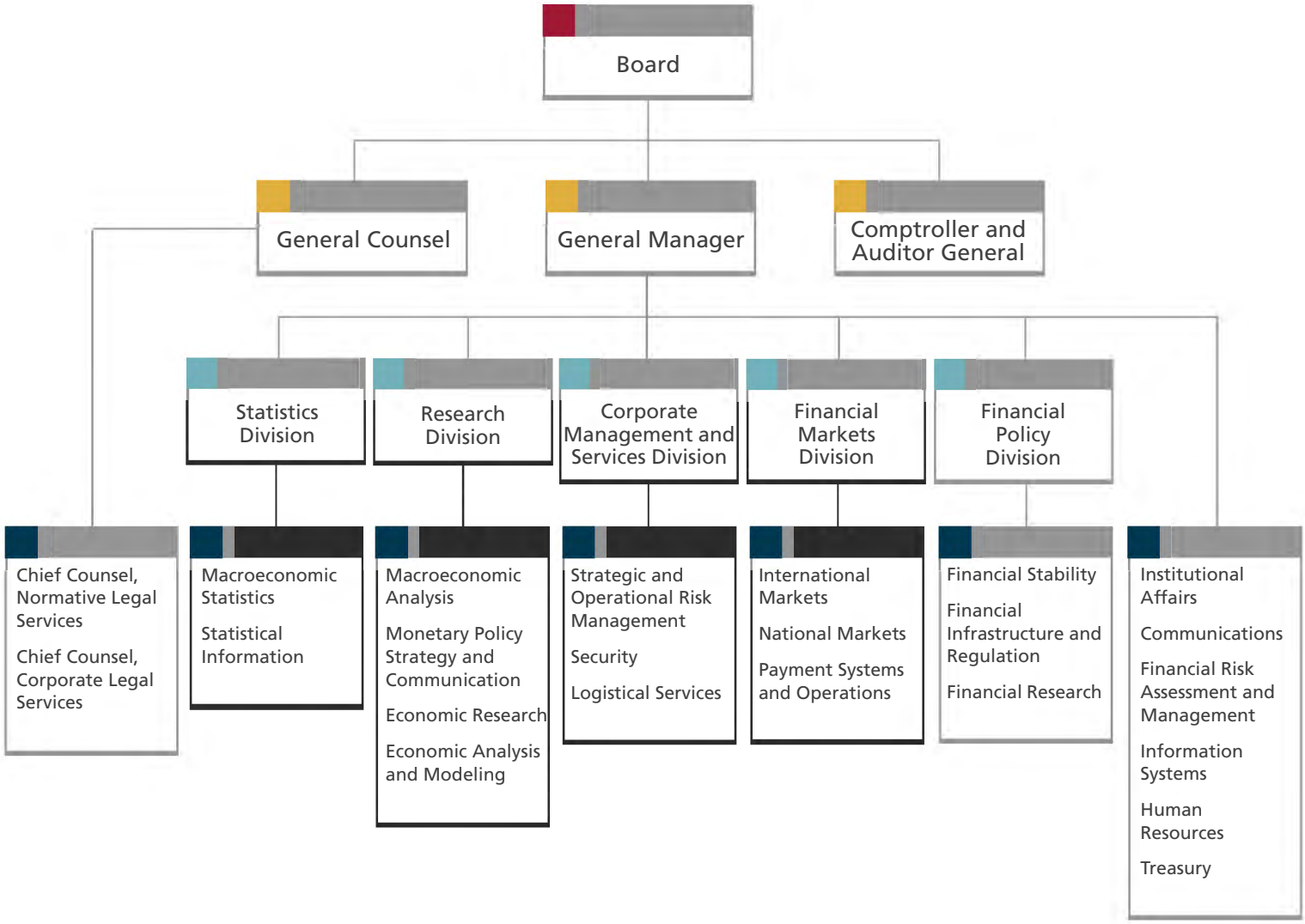
continued

Institution
Standard Chartered Securities Korea Limited, Seoul
Sumitomo Mitsui Banking Corporation, New York
Sumitomo Mitsui Trust Bank Ltd., New York
Svenska Handelsbanken Ab (Publ), New York
TD Securities (Usa) Llc.
The Bank of Montreal, Toronto
The Bank of New York Mellon, New York
The Bank of Tokyo-Mitsubishi UFJ Ltd., New York
The Chiba Bank Ltd., London
The Chiba Bank Ltd., New York
The Royal Bank Of Scotland Plc., London
The Shizuoka Bank Ltd., New York Branch
The Toronto Dominion Bank, Toronto
Ubs A,G., London
Ubs Limited, London
Ubs Securities Llc., New York
Wells Fargo Bank N.A., San Francisco
Wells Fargo Securities, Llc.
Westpac Banking Corporation, Sydney
Westpac Banking Corporation, Wellington
Zurcher Kantonalbank, Zurich

Source: Central Bank of Chile.

ORGANIZATIONAL STRUCTURE

AS OF 31 DECEMBER 2017



value recognition and promotion

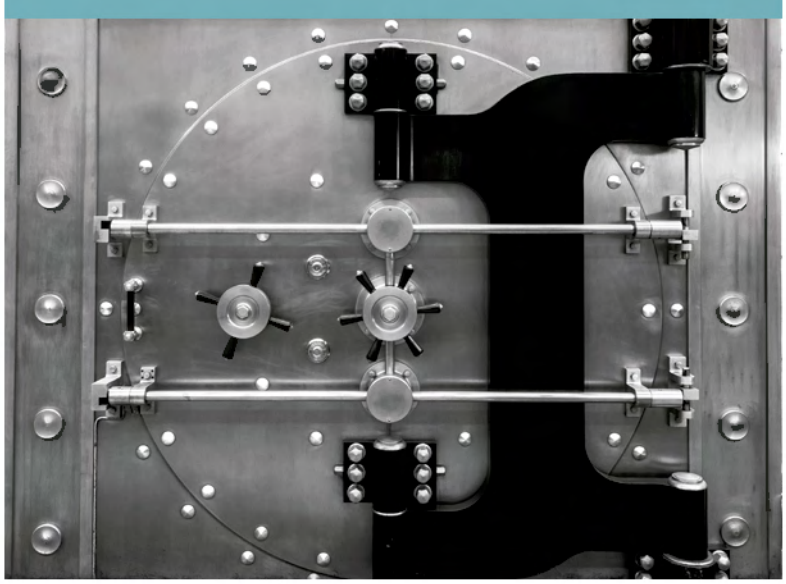
motivated and committed

personnel management

operational continuity

retention of talent

Employer of excellence

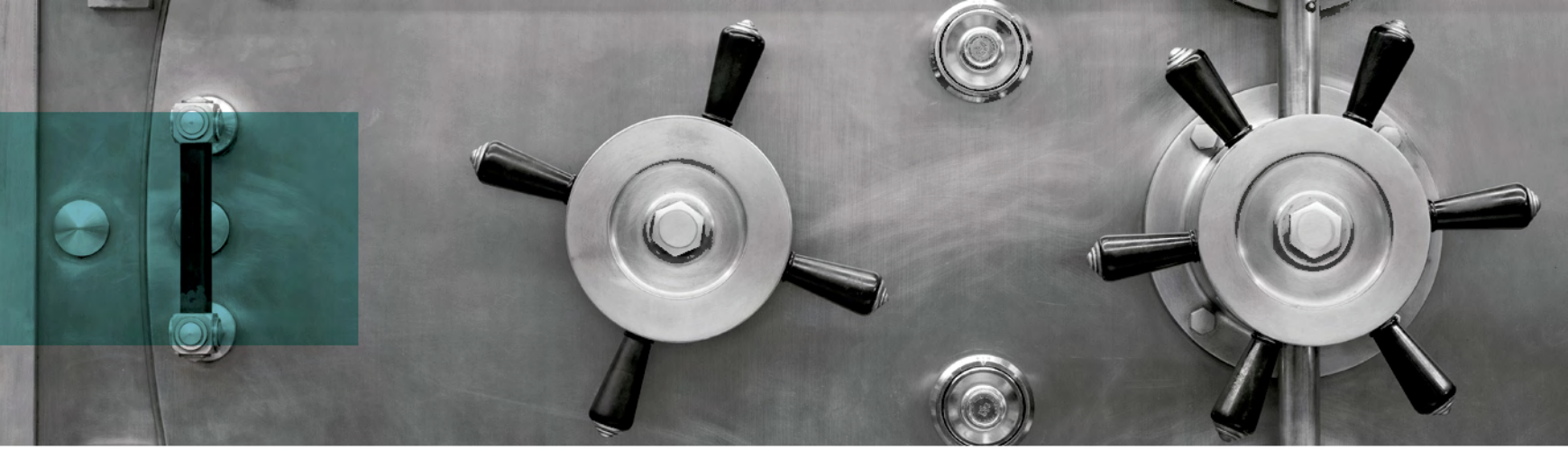


FINANCIAL STATEMENTS

STATEMENTS OF FINANCIAL POSITION
as of 31 December 2017 and 2016

Assets	Note	2017 Ch$ million	2016 Ch$ million
Foreign assets		24,100,688.4	27,181,581.1
Reserve assets	11	23,982,892.0	27,021,006.9
Monetary gold		6,305.8	6,070.8
Special drawing rights (SDR)		473,891.0	485,453.8
Reserve position in the International Monetary Fund (IMF)	12	154,491.6	143,497.2
Correspondent banks abroad	6	721,350.1	683,756.5
Investments in foreign currency:	11 b	22,625,028.3	25,691,282.3
Securities recorded at fair value through earnings		19,569,596.6	18,322,931.3
Held-for-sale securities		1,492,666.8	3,085,235.9
Held-to-maturity securities		1,562,764.9	4,283,115.1
Reciprocal loan agreements		1,296.8	10,014.5
Other assets		528.4	931.8
Other foreign assets		117,796.4	160,574.2
Shares of and contributions to the Inter-American Development Bank (IDB)		80,950.4	122,849.2
Shares of Bank for International Settlements (BIS)		36,846.0	37,725.0
Domestic assets		839,308.4	667,452.8
Domestic loans	13	302,947.8	12,501.8
Loans to banks and financial institutions		302,947.8	12,501.8
Transactions under specific legal regulations		536,360.6	654,951.0
General Treasury Transfers Law 18,401	14 a	305,069.6	299,945.0
Loan for subordinated liabilities of financial institutions (Laws 18,401 and 19,396)	14 c	231,291.0	355,006.0
Other assets		57,835.4	58,970.5
Property, equipment and intangible assets	15	43,077.3	41,605.6
Other securities		14,585.5	14,101.2
Transition assets		172.6	3,263.7
Total assets		24,997,832.2	27,908,004.4

Accompanying notes from 1 to 28 are an integral part of these financial statements.



STATEMENTS OF FINANCIAL POSITION
as of 31 December 2017 and 2016

Liabilities	Note	2017 Ch$ million	2016 Ch$ million
Foreign liabilities	16	768,875.8	790,794.1
Reciprocal loan agreements		41.7	49.9
Accounts with international organizations		52,250.6	57,681.3
Special drawing rights (SDR) allocations		716,583.5	733,062.9
Domestic liabilities		29,988,787.4	31,298,960.3
Monetary base	17	11,105,786.6	10,342,493.8
Banknotes and coins in circulation		8,970,283.8	8,651,831.2
Deposits from financial institutions (domestic currency)		1,527,426.8	1,690,662.6
Deposits for technical reserves		608,076.0	-
Deposits and obligations	18	4,046,317.0	5,842,324.2
Deposits and obligations with General Treasury		317,897.9	780,412.4
Other deposits and obligations		3,728,419.1	5,061,911.8
Notes issued by Central Bank of Chile	19	14,836,683.8	15,114,142.3
Central Bank of Chile bonds in UF (BCU)		5,996,960.3	6,777,119.7
Central Bank of Chile bonds in Chilean pesos (BCP)		3,669,482.4	4,037,484.6
Central Bank of Chile discountable promissory notes (PDBC)		5,100,493.5	4,206,282.1
Optional indexed coupons (CERO) in UF		51,121.4	66,314.1
Indexed promissory notes payable in coupons (PRC)		18,618.4	26,930.3
Other		7.8	11.5
Other liabilities		23,505.5	24,131.6
Provisions	20	20,168.1	19,203.8
Other securities		3,337.4	4,927.8
Net equity	21	(5,783,336.5)	(4,205,881.6)
Capital		(4,216,670.8)	(1,983,898.1)
Other reserves		17,101.8	10,789.2
Retained earnings		(1,583,767.5)	(2,232,772.7)
Total liabilities and equity		24,997,832.2	27,908,004.4

Accompanying notes from 1 to 28 are an integral part of these financial statements.

STATEMENTS OF COMPREHENSIVE INCOME
for the years ended 31 December 2017 and 2016

	Note	2017 Ch$ million	2016 Ch$ million
Net gain from international reserves	7a	175,675.1	213,716.6
Income		390,610.3	494,317.9
Interest income		311,577.5	312,609.9
Gain on sale of instruments recorded at fair value through earnings		53,311.3	168,893.6
Gain on sale of available-for-sale securities		22,702.2	12,108.4
Other		3,019.3	706.0
Expenses		(214,935.2)	(280,601.3)
Interest expenses		(2.9)	(1.5)
Loss on sale of instruments recorded at fair value through earnings		(148,342.7)	(216,442.7)
Fair value adjustments		(63,449.3)	(60,837.9)
Other		(3,140.3)	(3,319.2)
Net (loss) gain from other foreign transactions	7b	(28,668.0)	37,388.9
Income		9,161.8	39,729.4
Other income		9,161.8	39,729.4
Expenses		(37,829.8)	(2,340.5)
Interest expense		(3,760.8)	(614.0)
Other expenses		(34,069.0)	(1,726.5)
Net loss from domestic transactions	8	(657,630.3)	(774,429.0)
Income		28,864.1	46,996.2
Interest income and adjustments		24,318.2	39,222.6
Other income		4,545.9	7,773.6
Expenses		(686,494.4)	(821,425.2)
Interest expense and adjustments		(686,212.5)	(821,012.6)
Other expenses		(281.9)	(412.6)
Net loss gain on foreign exchange transactions	9	(977,379.9)	(1,623,174.1)
Gain on foreign exchange transactions		2,142,968.7	2,354,367.4
Loss on foreign exchange transactions		(3,120,348.6)	(3,977,541.5)
Issuance and distribution costs	10	(35,125.1)	(26,154.2)
Banknotes		(12,792.3)	(9,727.7)
Coins		(20,747.7)	(14,741.0)
Distribution		(1,585.1)	(1,685.5)
Personnel and administrative expenses		(56,849.7)	(56,065.5)
Personnel expenses		(36,353.3)	(35,587.9)
Administrative expenses		(18,588.2)	(18,619.6)
Provision for post-employment benefits	20	(1,908.2)	(1,858.0)
Other (expenses) and income		(3,789.6)	(4,055.4)
Depreciation and amortization	15	(2,754.0)	(3,433.4)
Taxes and contributions		(639.8)	(623.0)
Other		(395.8)	1.0
Loss for the period		(1,583,767.5)	(2,232,772.7)
Other comprehensive income		6,312.6	2,690.9
Other comprehensive (loss) income that will not be reclassified to profit or loss		(55.9)	223.7
Actuarial (loss) gain in provision for post-employment benefits		(55.9)	223.7
Other comprehensive income that may be reclassified to profit or loss		6,368.5	2,467.2
Fair value adjustments of available-for-sale securities		6,368.5	2,467.2
Total comprehensive income		(1,577,454.9)	(2,230,081.8)

Accompanying notes from 1 to 28 are an integral part of these financial statements.

STATEMENTS OF CHANGES IN EQUITY

for the years ended 31 December 2017 and 2016
(Ch$ million)

	Capital	Actuarial gain or loss reserve	Fair value reserve	Total other reserves	Retained earnings	Total
Balances as of 1 January 2016	(3,549,232.2)	(142.1)	8,240.4	8,098.3	1,565,334.1	(1,975,799.8)
Total comprehensive income:						
(Loss)	-	-	-	-	(2,232,772.7)	(2,232,772.7)
Other comprehensive income	-	223.7	2,467.2	2,690.9	-	2,690.9
Total comprehensive income (loss)	-	223.7	2,467.2	2,690.9	(2,232,772.7)	(2,230,081.8)
Capitalization of 2015 profit	1,565,334.1	-	-	-	(1,565,334.1)	-
Balances as of 31 December 2016	(1,983,898.1)	81.6	10,707.6	10,789.2	(2,232,772.7)	(4,205,881.6)
Balances as of 1 January 2017	(1,983,898.1)	81.6	10,707.6	10,789.2	(2,232,772.7)	(4,205,881.6)
Total comprehensive income:						
(Loss)	-	-	-	-	(1,583,767.5)	(1,583,767.5)
Other comprehensive income	-	(55.9)	6,368.5	6,312.6	-	6,312.6
Total comprehensive income	-	(55.9)	6,368.5	6,312.6	(1,583,767.5)	(1,577,454.9)
Capitalization of 2016 deficit	(2,232,772.7)	-	-	-	2,232,772.7	-
Balances as of 31 December 2017	(4,216,670.8)	25.7	17,076.1	17,101.8	(1,583,767.5)	(5,783,336.5)

Accompanying notes from 1 to 28 are an integral part of these financial statements.

STATEMENTS OF CASH FLOWS
for the years ended 31 December 2017 and 2016

	Note	2017 Ch$ million	2016 Ch$ million
Cash flows from operating activities			
Foreign reserves		2,175,144.8	(1,224,488.8)
Purchase (sale) of securities at fair value		(2,132,895.1)	616,743.3
(Sale) purchase of available-for-sale securities		1,398,902.0	(1,281,847.2)
(Investments in) redemption of held-to-maturity securities		2,575,360.0	(903,323.4)
Interests and commissions received for international reserves		328,254.3	329,735.5
Interests paid in foreign transactions		(3.0)	-
Taxes paid for investments in reserves		(3,178.4)	(3,514.1)
Cash receipts for reciprocal loan agreements		8,639.1	17,496.2
Interest receipts for reciprocal loan agreements		66.8	221.6
Interest payments for reciprocal loan agreements		(0.9)	(0.7)
Domestic assets		(147,862.8)	128,888.3
Cash receipts (disbursements) for loans to banks and financial institutions		(290,291.2)	(12,466.4)
Interests and adjustments received for loans to financial institutions		425.0	740.4
Cash receipts for subordinated obligation with financial institutions		79,459.7	76,971.4
Interests and adjustments received for subordinated obligations		62,543.7	63,642.9
Domestic liabilities		(2,173,790.5)	947,467.8
(Maturity)/Placement of notes issued		(188,198.0)	1,762,806.0
Interests and adjustments paid for notes issued		(702,152.6)	(869,185.7)
Increase/(Decrease) in deposits and obligations in Chilean pesos		854,440.5	(1,067,234.3)
Interests and adjustments paid for deposits and obligations		(60,422.2)	(95,263.3)
(Decrease)/increase in deposits and obligations in foreign currency		(2,077,458.2)	1,216,345.1
Other cash flows		(85,882.9)	(93,115.9)
Cash payments for goods and services		(94,574.5)	(85,965.9)
Net cash flows for arbitrage of currencies		5,982.9	(14,521.2)
Cash receipts as fiscal agent and other income		3,479.5	4,255.0
Movements in international organizations		(770.8)	3,116.2
Net cash used in operating activities		(232,391.4)	(241,248.6)

Accompanying notes from 1 to 28 are an integral part of these financial statements.

STATEMENTS OF CASH FLOWS

for the years ended 31 December 2017 and 2016

continued

	Note	2017 Ch$ million	2016 Ch$ million
Cash flows from investing activities			
Movements, IMF		(13,542.9)	321,440.0
Dividend received, BIS		825.7	595.4
Proceeds from sale of property and equipment		22.7	-
Acquisition of property and equipment	15	(2,815.4)	(8,586.4)
Acquisition of intangible assets	15	(1,459.2)	(74.3)
Net cash generated from investing activities		(16,969.1)	313,374.7
Cash flows from financing activities			
Net increase in banknotes and coins in circulation		318,452.6	234,137.6
Net cash generated from financing activities		318,452.6	234,137.6
Changes in cash and cash equivalents		69,092.1	306,263.7
Effect of exchange rate fluctuations on cash and cash equivalents		(31,941.5)	(49,753.0)
Cash and cash equivalents at the beginning of the reporting period		684,865.1	428,354.4
Cash and cash equivalents at 31 December	6	722,015.7	684,865.1

Accompanying notes from 1 to 28 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

as of 31 December 2017 and 2016

Note 1
INCORPORATION AND DESCRIPTION OF BUSINESS

Central Bank of Chile was formed on 22 August 1925, by Decree Law 486, the Bank is a constitutionally autonomous entity, has full legal capacity, its own assets and indefinite duration, created in accordance with Articles 108 and 109 of the Political Constitution of Chile and ruled by its Basic Constitutional Act.

Central Bank of Chile objective is to monitor the stability of both the Chilean currency and the normal functioning of domestic and foreign payments.

In order to meet its objectives, Central Bank of Chile regulates the amount of money and credit in circulation, executes credit transactions and international exchange, and dictates regulations on monetary credit, and financial and international exchange matters.

Additionally, the Bank is exclusively empowered to issue banknotes and to mint coins.

The Bank is domiciled in Santiago de Chile, and its main office is located at 1180 Agustinas street.

Note 2
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of preparation of the financial statements

These financial statements have been prepared in conformity with the "Policies of presentation and preparation of financial reports of Central Bank of Chile" approved by Central Bank of Chile Board, pursuant to Resolution 1456-01 dated 15 January 2009 and 1519-01 dated 14 January 2010, and 1867-01 dated 20 November 2014, having a favorable report by the Superintendence of Banks and Financial Institutions, pursuant to Section 75 of Central Bank of Chile Basic Constitutional Act. The policies approved by the Board are consistent with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB).

The presentation of these financial statements is framed within an economic and accounting framework that fairly reflects the financial position of Central Bank of Chile, and at the same time, contributes to the economic analysis of Central Bank of Chile transactions by clearly identifying whether they are undertaken by domestic or foreign agents. With this information it is possible to determine Central Bank of Chile share in the domestic supply of monetary and credit assets and the related effects on Central Bank of Chile foreign creditor position. For this reason, the economic concepts of international reserves and currency issuance are shown under the captions reserve assets and monetary base liabilities, respectively.

The translation of these financial statements is provided as a free translation from the Spanish original, which is the official and binding version. Such translation has been made solely for the convenience of non-Spanish readers.

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis. The abovementioned excludes transactions corresponding to foreign investments in financial instruments that are reported at their fair value through net income and available-for-sale securities through equity, which basis of measurement has been performed taking their fair value as reference.

The methods used to measure fair values are presented in note 3.

(c) Functional and presentation currency

As Central Bank of Chile main objective is to monitor the stability of the Chilean currency, which implies that open-market transactions play a significant role in the development of the monetary policy, being its main activity the issuance of banknotes and coins. The Chilean peso has been defined as the functional and presentation currency for the financial statements.

The amounts in such statements are stated in millions of Chilean pesos, while the amounts of these notes are stated in millions of Chilean pesos or U.S. dollars, as applicable, rounded to the nearest decimal.

(d) Transactions in foreign currency and foreign currency translation

Central Bank of Chile functional currency is the Chilean peso. Consequently, all balances and transactions denominated in currencies other than the Chilean peso are considered to be denominated in a "foreign currency". The balances of the financial statements expressed in these currencies are translated into Chilean pesos as follows:

(i) U.S. dollars are translated into Chilean pesos at the closing date "observed U.S. dollar" exchange rate pursuant to Section 44 of the Basic Constitutional Act, that governs Central Bank of Chile referred to under No. 6 of Chapter I in the "General Provisions" of the *Compendium of Foreign Exchange Regulations* (*Compendio de Normas de Cambios Internacionales*).

(ii) Assets and liabilities stated in Chilean minted gold, are valued at the average London morning quotation of the "Gold Fixing" rate (U.S. dollars per fine troy ounce), in the morning of the closing business day of the financial statements.

(iii) Translation of foreign currencies other than the U.S. dollar is done at the exchange rates published daily by Central Bank of Chile in the *Official Gazette*, which are always based upon the period-end "observed U.S. dollar" rate.

(iv) Special Drawing Rights (SDR) are adjusted for at the exchange rates for each of the business days of the month, reported by Central Bank of Chile, except for the last business day of the month in which the exchange rate reported by the International Monetary Fund (IMF) is considered.

The results from the purchase and sale of foreign currency, as well as the differences arising from the update of the balances in foreign currency, as a result of the variation of the exchange rates of such foreign currencies compared to the Chilean peso, are recorded as profits or losses for the year.

The principal exchange rates used as of each year-end are as follows:

	2017 Ch$	2016 Ch$
United States dollar (observed exchange rate)	615.22	667.29
Euro	735.21	698.51
Canadian dollar	488.81	493.74
Australian dollar	479.37	480.93
Special drawing rights (SDR)	876.16	897.06

(e) Statement of cash flows

The following factors are taken into account when preparing the statement of cash flows:

(i) Cash flows: cash and cash equivalents inflows and outflows. Cash equivalents are highly liquid short-term investments and low risk of changes in value, as: deposits in foreign banks and cash balances in foreign currency and deposits in domestic banks.

(ii) Operating activities: correspond to normal activities carried out by Central Bank of Chile and other activities that cannot be classified as investing or financing activities.

(iii) Investing activities: correspond to the acquisition, disposal or disposition by other means of long-term assets and other investments not included in cash and cash equivalents.

(iv) Financing activities: these activities generate changes in the size and composition of net equity and liabilities that are not part of operating or investing activities.

(f) Interest income and expenses, adjustments and commissions

Interest income and expenses, adjustments and commissions are recognized in earnings for the year when earned. Interest is recognized on the basis of its effective rate.

(g) International reserves measurement criteria

International reserves are liquid assets in foreign currency held by Central Bank of Chile. They are instruments supporting monetary and foreign exchange policies, in order to meet Central Bank of Chile objective of safeguarding currency stability and the normal functioning of internal and external payment systems. Reserve assets comprise those external assets under the control of the monetary authority, which can dispose them immediately in order to fund the imbalances of the balance of payments and to indirectly regulate the magnitude of those imbalances.

Investments in foreign financial instruments are recognized at the date of the purchase at its fair value. In addition, they are classified in accordance with IFRS, in the following categories and composition:

(i) Investments recorded at fair value through earnings

Includes bonds issued by foreign governments, mid-term bonds issued by the Bank for International Settlements (BIS), treasury bills, discount notes, inflation-linked bonds, secured bonds from public institutions issued by German banks, agency non-prepayable bonds, agency prepayable bonds, agency bills, mortgage backed securities MBS, and agency discount notes, floating rate notes and derivatives (interest rate futures).

The principle considerations used to classify instruments focus on their high liquidity. They are recorded at fair value and their changes are recognized directly in earnings. The methods used to measure fair values are described in note 3.

(ii) Available-for-sale securities

Commercial papers, short-term investments at fixed rate with BIS (discounted and at interest rate, both tradable with BIS) and BISIP (collective investments through BIS).

These are investments in financial instruments, which when certain market conditions are met they may become effective prior to their maturity dates. These are recorded at their fair value, and changes are directly recognized in equity until the investment is disposed of or impaired, when results in accumulated gains or losses previously recorded in equity are recognized in earnings. The methods used to measure fair values are described in note 3.

(iii) Held-to-maturity securities

Term and overnight deposits. Correspond to investments in financial assets that the entity has the intent and ability to hold until maturity; they are valued at amortized cost using the effective interest method. These financial assets are not affected by transaction costs.

(iv) Other reserve assets

(iv.1) Monetary gold: corresponds to gold held as international reserve, expressed in Chilean minted gold, is valued at the average quotation of the London Gold Fixing (U.S. dollar per fine troy ounce) and the differences arising from updating the gold positions are recorded as profit or loss for the year.

(iv.2) Special drawing rights (SDR) correspond to reserve assets, equivalent to foreign currencies, assigned by the International Monetary Fund (IMF) to the member countries proportionally to the installment paid and valued in Chilean pesos considering the current parity reported by the International Monetary Fund.

(iv.3) Reserve position in the International Monetary Fund (IMF): corresponds to the net difference between the assets (payments made to the IMF for subscription, and loans granted by the Central Bank of Chile to the IMF for the participation in the financing program "New Arrangement to Borrow" - NAB) and liabilities (deposits maintained by the IMF in domestic currency) and is classified as a held-to-maturity investment, measured at the cost indexed to Special Drawing Rights (SDR).

(iv.4) Reciprocal Loan Agreements (debit): represent the amount owed to the Central Bank of Chile by the central banks comprising Aladi's Agreement on Reciprocal Payments and Credits for the exports made by Chilean entities through such method. Their classification corresponds to non-derivative, held-to-maturity financial instruments, measured at amortized cost using the effective interest method.

(h) Shares and contributions to the Inter-American Development Bank (IDB) and contributions to the International Monetary Fund (IMF)

As of 31 December 2016, the Bank maintained shares of Ordinary Capital and contributions to the Fund for Special Operations (FSO) of the Inter-American Development Bank (IDB).

On 1 September 2016, the Board of Governors of the IDB agreed on the transfer of assets and liabilities from the Fund for Special Operations (FSO) to shares of Ordinary Capital of the IDB starting from 1 January 2017 through Resolution AG-9/16 "Proposal for Sustaining Concessional Assistance by Optimizing the IDB's Balance Sheets."

The accounting treatment of the previously mentioned shares and contributions is in conformity with Article 3 of DL 2943 dated 1979, according to which such shares and contributions as well as the notes evidencing them, must be recorded by the Central Bank of Chile as investments with a charge to its own resources for accounting purposes.

The shares of Ordinary Capital of the Inter-American Development Bank and contributions to the International Monetary Fund, all from the General Treasury are measured at their acquisition cost or contributions plus the adjustments reported by each of the institutions, where appropriate.

(i) Bank for International Settlements (BIS) Shares

During 2003, Central Bank of Chile Board Resolutions 1073-04 dated 10 July 2003 and 1084-02 dated 16 September, 2003, authorized the incorporation of the Central Bank of Chile as a member of the Bank for International Settlements (BIS). On 26 September 2003, in accordance with these resolutions, Central Bank of Chile acquired 3,000 shares of the BIS for SDR42,054,000 which are valued at acquisition cost and are shown under "Other Foreign Assets." During 2017, dividends were received in the amount of US$1.2 million (US$0.9 million in 2016).

(j) Domestic loans

Domestic loans are non-derivative financial assets that correspond to loans granted in Chile, classified as held-to-maturity securities, stated with interests and adjustments accrued at year-end and measured at amortized cost pursuant to the effective interest rate method, and are not affected by transaction costs.

Non-adjustable loans are shown at their original value or at their latest renewal value and adjustable balances or denominated in foreign currency include the accrued exchange rate and adjustments at the reporting date.

(k) Transactions under specific legal regulation

Correspond to non-derivative financial assets subject to specific regulatory and legal restrictions, which are classified as held-to-maturity securities and are measured at amortized cost pursuant to the effective interest rate method, and are not affected by transaction costs.

(l) Property, equipment and intangible assets

Property and equipment are mainly measured at acquisition cost, net of accumulated depreciation and any accumulated impairment losses. The goods that have met their useful life are stated at their residual value considering market reference prices. Depreciation is calculated on a straight-line basis.

Intangible assets are measured at acquisition cost, net of accumulated amortization and any accumulated impairment losses. Amortization is calculated on a straight-line basis. In 2017 and 2016, the Bank recognized as intangible assets the costs related to the acquisition of licenses and development of the Open Market Transaction System - SOMA.

Depreciation and amortization for 2017 and 2016 have been calculated considering the following estimated useful lives:

	Years	
	2017	2016
Buildings	50 to 80	50 to 80
Facilities	10 to 20	10 to 20
Furniture and other equipment	5 to 10	5 to 10
Computer equipment	3 to 5	3 to 5
Vehicles	5	5
Intangible assets	5	5

(m) Monetary base

Mostly include liabilities of Central Bank of Chile freely-circulating banknotes and coins, plus deposits made by the financial system in Central Bank of Chile.

(n) Deposits and obligations

Deposits received and obligations are financial liabilities for deposits and other transactions made with the General Treasury and financial institutions, and which are not affected by transaction costs. Subsequently, they are measured at amortized cost pursuant to the effective interest rate method with an effect in earnings. Unadjustable balances are stated at nominal value. Adjustable balances or those denominated in foreign currency include the effect of the accrued exchange rate and adjustments at the reporting date.

(o) Notes issued by the Central Bank of Chile

Notes issued by the Central Bank of Chile are financial liabilities issued in order to adopt the decisions of the monetary and debt policy, initially measured at fair value, and are not affected by transaction costs. Subsequently, they are measured at amortized cost pursuant to the effective interest rate method with the effect recorded in earnings. Unadjustable balances are stated at their nominal value. Adjustable balances include the effect of the accrued adjustments at the reporting date.

Notes issued comprise of: Central Bank of Chile bonds in UF (BCU), Central Bank of Chile bonds in Chilean pesos (BCP), Central Bank of Chile discountable promissory notes (PDBC), Indexed-promissory notes payable in coupons (PRC), and Optional indexed coupons (CERO) in UF.

(p) Impairment

(i) Financial assets

Impairment standards will be applied on financial assets other than those measured at fair value through earnings. For cases where the current value of estimated cash flows, discounted at the effective interest rate, is lower than the amount recognized in the accounting records, their impairment is recognized in earnings.

(ii) Non-financial assets

The carrying amounts of the Bank's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

(q) Employee benefits

(i) Long-term benefits

Post-employment benefits correspond to employee benefits which are payable after the completion of employment in Central Bank of Chile, as stipulated in the collective agreement between Central Bank of Chile and the Labor Union of Central Bank of Chile, signed on 26 June, 2015 and in effect starting from 1 July, 2015 through 30 June, 2019; for special resolutions approved by the Board and for special benefits provided to retired employees of the Former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile. These benefits include severance indemnities, special indemnity Resolution 1414-01 dated 5 June 2008, special supplementary severance indemnity under the retirement plan per Resolution 1651-06 dated 29 December, 2011 and special benefits to retired employees of the Former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile.

An estimate is made through an actuarial calculation that considers demographic and financial variables. It is measured at the present value of all future payments using an annual discount rate, affected by the expected duration of employment and life expectancy of beneficiaries.

The actuarial calculation is based on the following assumptions:

- Mortality rate: for 2017 the Central Bank of Chile used the RV-2014(RV-2014 for 2016) mortality table to determine the expected lives in the calculation of benefits associated with severance indemnity payments, post-employment benefits associated with the retirement plan's health plan and benefits of the Former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile.

- Employee turnover: The probabilities of remaining an employee of Central Bank of Chile were calculated on the basis of the tables prepared by Central Bank of Chile organized in tranches by years of service.

- Salary growth rate: calculated as the annual average composed of the salary growth rate for a five-year period of 5.71%.

- Discount rate: Central Bank of Chile used the nominal rate for BCP instruments at 10 years at the calculation date. For 2017, the discount rate was 4.62% (2016: 4.50%).

(ii) Short-term benefits

Accrued vacations: The annual cost of employee vacations is recognized in the financial statements on an accrual basis.

(r) Provisions and contingent liabilities

Provisions are liabilities for which there exists uncertainty related to their timing or amount. These provisions are recognized in the statement of financial position when both of the following requirements are met:

- A present obligation arising from past events; and
- At the date of the financial statements it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate of the amount of the obligation can be made.

A contingent liability is:

- An obligation that arises from past events and whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the control of Central Bank of Chile; or

- A present obligation, as a result of past events, which has not been recognized because:

- It is not probable that an outflow of economic benefits will be required to settle the obligation; or

- The amount cannot be estimated reliably.

(s) Financial derivative instruments

Financial derivative contracts corresponding to interest rate futures and forward exchange contracts that are initially recognized in the statement of financial position at fair value at the date in which the contract is entered into. Derivative contracts are reported as an asset when their fair value is positive and as a liability when is negative, are included in the captions "Other securities" in asset and liability, respectively, and are engaged to hedge currency and interest rate risk exposure.

Central bank of Chile does not use accounting hedges; accordingly, when entering into a derivative instrument, this is accounted for as held-for-trading derivative instrument (measured at fair value through profit or loss).

(t) Use of estimates and judgments

The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis by Central Bank of Chile senior management in order to quantify some assets, liabilities, income, expenses and uncertainties. The changes from accounting estimates are recognized in the period in which the estimate is revised and in any future period affected.

In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are described in the following notes:

- Note 2(l) Property, equipment, and intangible assets, determination of useful life, depreciation or amortization and residual value.
- Note 3 Methodology applied for the measurement of fair value.

- Note 14(b) *Caja Central de Ahorros y Préstamos* and *Asociación Nacional de Ahorro y Préstamo*.
- Note 20 Provisions, including severance indemnity and post-employment benefits.

(u) Issued but not yet effective IFRSs

A number of new accounting standards are applicable to annual periods beginning on or after 1 January, 2018. Early adoption is permitted. However, the following standards and amendments have not been early adopted by Central Bank of Chile in preparing these financial statements.

Standards that may be relevant for the Bank are detailed below.

IFRS 9 "Financial Instruments"

This standard establishes new requirements for recognizing and measuring financial assets, financial liabilities, and certain purchase or sale contracts of non-financial items. This standard supersedes IAS 39 "Financial Instruments: Recognition and Measurement," and is expected to have an impact on the Bank's financial statements at the initial application date. The main impacts are explained below.

1. Classification and measurement of financial assets and financial liabilities

- Financial assets

IFRS 9 includes a new approach to classify and measure financial assets, which reflects the business model under which the assets are managed, as well as the nature of cash flows.

The standard includes three main categories to classify financial assets: measured at amortized cost, at fair value through other comprehensive income (FVTOCI), or at fair value through profit or loss (FVTPOL). The standard eliminates the existing categories under IAS 39, held to maturity, loans and receivables, and available for sale.

Based on its assessment, Central Bank of Chile believes that these new classification requirements will have no material impact on its accounting and measurement of foreign investments, which are in general measured at fair value. There will be a reclassification to a greater extent from instruments at fair value through profit or loss (IAS 39) to the new classification of fair value through equity (IFRS 9); this will imply that all gains or losses at fair value will be reported in other comprehensive income, and will be recognized in profit or loss at their date of disposal. As a result of the elimination of the available-for-sale classification, investments will be reclassified at amortized cost and fair value through profit or loss.

Investments in foreign currency

Financial assets	Classification under IAS 39	Classification under IFRS 9
Bonds and notes at nominal value Discounted commercial paper (General Treasury notes) Inflation-adjusted bonds Short-term bonds issued by the BIS Floating rate notes Derivative instruments (FX and Futures) Mortgage-backed securities	Securities recorded at fair value through profit or loss	Fair value through other comprehensive income Fair value through profit or loss

Financial assets	Classification under IAS 39	Classification under IFRS 9
Commercial paper Short-term investments at fixed rate with the BIS Collective investments through BIS (BISIP)	Held-for-sale securities	Amortized cost Fair value through profit or loss

Financial assets	Classification under IAS 39	Classification under IFRS 9
Term deposits Overnight and weekend deposits	Held-to-maturity securities	Amortized cost

Other reserve assets will not be affected by the application of IFRS 9 with respect to their current accounting treatment.

Other foreign assets

Financial assets (equity securities)	Classification under IAS 39	Classification under IFRS 9
Shares of and contributions to the Inter-American Development Bank (IDB) Shares of Bank for International Settlements (BIS)	Amortized cost	Fair value through other comprehensive income

For financial assets: For shares and contributions to the BID and shares of the Bank for International Payments, Central Bank of Chile has made the irrevocable option of presenting in other comprehensive income the subsequent changes in fair values of investments in equity securities which, being within the scope of IFRS 9, are not held for trading. The aforementioned option will imply the recognition of the dividends from such investments in profit or loss.

• Financial liabilities

Financial liabilities will not be affected by the application of IFRS 9 with respect to their current accounting treatment.

2. Impairment of financial assets

IFRS 9 replaces the "incurred loss" model of IAS 39 with the "expected credit loss" (ECL) model. This will require considerable judgment with respect to how changes in economic factors affect ECL, which will be determined on a weighted average basis.

The new impairment model will be applicable to financial assets measured at amortized cost or at fair value through other comprehensive income, except for investments in equity securities.

Under IFRS 9, loss estimates are measured using one of the following bases:

- 12-month expected credit losses: These are expected credit losses that may result from default events within 12 months subsequent to the reporting date; and
- Lifetime expected credit losses: These are expected credit losses that may result from potential default events during the life of the financial instrument.

The measurement of lifetime expected credit losses applies if, at the reporting date, the credit risk of a financial asset has significantly increased from the initial recognition whereas measurement of 12-month expected credit losses applies if such risk has not increased. The entity may determine that the credit risk of a financial asset has not significantly increased if the asset has low credit risk at the reporting date.

Due to the impairment model established in IFRS 9, Central Bank of Chile believes that, from its effective date, it will incur impairment losses that will not be significant considering the low credit risk of its investments. Based on the assessment conducted by the Bank, the estimated impact of impairment losses on the Bank's equity will be approximately Ch$6,152.2 million (US$10.0 million).

3. Transition

Central Bank of Chile will elect the exemption that allows it to not restate comparative information from prior periods concerning changes in classification and measurement (including impairment). The differences in carrying amounts of financial assets and liabilities arising from the adoption of IFRS 9 will be recognized in retained earnings (accumulated deficit) as of 1 January 2018.

IFRS 15 "Revenue from Contracts with Customers"

Beginning on 1 January 2018, the Bank must adopt IFRS 15 "Revenue from Contracts with Customers", which establishes a full conceptual framework to determine if, when and how much revenue should be recognized. Based on its assessment and considering the Bank's nature and purpose, no significant impact is expected from the adoption of such standard.

IFRS 16 "Leases"

Beginning on 1 January 2019, the Bank must adopt IFRS 16, which replaces the following guidelines on leases: IAS 17 "Leases", IFRIC 4 "Determining whether an Arrangement Contains a Lease," SIC 15 "Operating Leases – Incentives," SIC 27 "Evaluating the Substance of Transactions Involving the Legal Form of a Lease." The main effects of such standards applies to the lessee accounting, mainly because of the removal of the dual model of accounting: operating or finance lease, i.e., the lessee should recognize a "right to use an asset" and a liability for the lease (the present value of future payments of leases). For the lessor, the standard maintains the current practice, i.e., lessor continues to classify finance and operating leases. At the reporting date, Management has established a program for reviewing the possible impact resulting from the adoption of such Standard.

Additionally, other standards have been issued but are not yet effective, which address matters that neither affect nor will affect the Bank's current transactions.

Note 3
METHODOLOGY APPLIED FOR THE MEASUREMENT OF FAIR VALUE

The methodology for the calculation of fair value is applied to financial instruments held as foreign investments, classified as securities at fair value through profit or loss, and available-for-sale securities.

The fair value of international reserve securities is classified by level as shown in note 11:

- Level 1, fair value measurements using quoted prices (unadjusted) in active markets for identical assets and liabilities, for which the Bank has the ability to access at the measurement date.
- Level 2, inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3, fair value measurements using unobservable inputs for the asset or liability.

The management of international reserves is performed through a computer system that includes a methodology for the calculation of fair value. The methodology distinguishes two types of calculation to establish the fair value: priced and non-priced securities.

(a) Priced securities (source: Bloomberg)

The system uses the market prices obtained from Bloomberg at the closing of current day transactions. The price corresponds to *PX Mid = (PX Bid + PX Last)/2*.

Where:

- *PX Mid:* Average price.
- *PX Bid:* The last purchase price available for an issuance in a particular day.
- *PX Last:* The last price at which an issuance has been measured in a particular day.

On the other hand, the system calculates the gains and losses from investments on a daily basis using the following formula for 2017 and 2016:

- *IR Profit/Loss = Total Gain Loss - Accrued Interest – FX Gain/Loss*

Where:

- *IR Profit/Loss:* Interest gain/loss due to price and reference rate changes.
- *Total Gain Loss:* Total gains and losses.
- *Accrued Interest:* Portion over the next coupon payment accrued from the last coupon until the calculation date.
- *FX Gain/Loss:* Gain/Loss due to the effects of foreign currency exchange differences.

(b) Non-priced securities (reference rate)

In regard to the purposes of compliance control, the change in the market value of those securities that do not have any quoted prices, it will only reflect the straight-line accrual of the premium/discount over the life of the transaction.

The abovementioned, completely removes the effect in the measurement resulting from the changes in the rates (Libid or Libor) and the effect is similar to what happens with the treatment of deposits.

For financial assets and financial liabilities not recognized at fair value, fair value will be disclosed collectively in groups to allow comparison with the related carrying amounts, as shown in note 11 (c).

Note 4
CHANGES IN ACCOUNTING POLICIES

As of 31 December 2017, the accounting policies have been consistently applied in relation to the year ended 31 December 2016.

Note 5
FINANCIAL INSTRUMENT RISKS

The goal of Central Bank of Chile is to monitor the stability of the Chilean currency; i.e. maintain a low and stable inflation rate over time. Additionally, the Bank promotes the stability and effectiveness of the financial system, safeguarding the normal performance of internal and external payments.

In order to meet that goal, Central Bank of Chile has its international reserves, liquid assets in foreign currency which are mainly comprised of financial instruments that are traded and kept in custody abroad such as bonds and government notes, bank deposits, among others.

Additionally, Central Bank of Chile implements its monetary policy through the definition of an objective level for the nominal inter-bank interest rate, known as the Monetary Policy Rate (*Tasa de Política Monetaria*, TPM in Spanish). In order for the inter-bank rate to be determined at this level,

Central Bank of Chile regulates the availability of liquidity (or reserves) of the financial system through several financial instruments related to the management of debt and open-market transactions made by the local market through the issuance of notes and term deposits received.

Central Bank of Chile financial risks are related to those risks arising from managing the asset and liability portfolio and their effect on the Bank's equity. Such risks can be classified as: Market risk, Credit risk, Liquidity risk, and Operational risk.

Financial risk management is established and based on general policies approved by Central Bank of Chile Board. In this respect, the definition of guidelines and assets and debt exposure limits are proposed to the General Management and the Board by the Management of the Financial Markets Division for their approval.

International Market Management and Domestic Market Management, which report to the Financial Markets Division, are responsible for implementing the policies established by the Board. While, within the same hierarchical line, the Management of Operations and Payment Systems records, processes and performs the settlement of transactions. Additionally, they manage the information systems in which these are carried out.

Financial Risk Management and Evaluation Management monitors the compliance with the established limits, measures management results and risks and reports them to the Manager of the Financial Markets Division and the General Management. In addition, the Bank' General Auditor, which reports directly to the Board, assesses the effectiveness and efficiency of the internal control, risk management and governance of the financial asset and liability portfolio process.

Finally, Central Bank of Chile Audit and Compliance Committee, which is an external advisor entity for the Board, is responsible, among other functions, for reporting on the effectiveness of the systems and the internal control procedures used in the financial asset and liability portfolio management, and assesses the reliability, integrity and timeliness of the information of the financial statements.

(a) Market risk

Market risk is the risk of potential losses from changes affecting the price or final value of a financial instrument or group of financial instruments. Risks are identified mainly by fluctuations in currencies and interest rates. Market risk affecting Central Bank of Chile statement of financial position is dominated by international reserves mainly due to the increased volatility of currencies composing their investments, while for liabilities, the greatest impact arises from fluctuations in the inflation-adjusted unit which impacts the long-term debt.

Market risk of international reserves is limited by the investment policy establishing maturity and composition margins of currencies around referential parameters of the portfolios and through the diversification of currencies, securities and investment periods. Market risk is monitored through the daily term and detail by currency and through the follow-up of Value at Risk (VaR) and risk related to the Referential Buyer (Tracking Error or TE).

Table 5.1 sets out the different monitored market risk measurements.

TABLE 5.1
MARKET RISK, INVESTMENT PORTFOLIO AS OF 31 DECEMBER 2017 AND 2016

		2017	2016
Amount (Ch$ million)*		21,576,765.5	22,401,089.9
Length (months)*	Portfolio	22.4	23.8
	Departure	-1.5	-0.1
Breakdown by currency (%)	US$	63.5	64.6
	EUR	16.6	16.3
	JPY	0.3	0.5
	Other	19.6	18.6
VaR Internal Investment Portfolio**	Absolute (%)	1.6	2.5
	Tracking Error (bp)	9.2	11.2
VaR External Investment Portfolio Blackrock*****	Absolute (%)	3.1	5.2
	Tracking Error (bp)	53.9	26.9
VaR External Investment Portfolio Amundi*****	Absolute (%)	2.9	4.9
	Tracking Error (bp)	65.2	89.4

Source: BCCh.

* The amounts correspond solely to the Investment Portfolio portion within the International Reserves. We do not consider amounts related to the Cash Portfolio or Other Assets.

** Value at Risk (VaR) and Tracking Error (TE): a parametric estimate methodology for VaR is used through a portfolio decomposition in risk factors related to changes in currencies, fiscal rates and spread. For those factors, we have developed a variance and covariance matrix, using a data window of 550 days, with an exponential decline factor of 0.94. The VaR is presented with a confidence level of 84%, equivalent to a standard deviation. VaR and TE are measured in U.S. dollars and are presented relative to the Investment Portfolio.

For open-market transactions, this risk is mainly associated with changes in the market value of bonds and promissory notes issued by Central Bank of Chile, and the change in value of collaterals received in liquidity injection transactions. For collaterals the risk of value loss is mitigated by using margins and haircuts that write-down their value and allow the effective amount lent to be lower than the collateral received. For the placement of bonds and promissory notes, risk is mitigated in line with the provisions in current legislation contained in the *Compendium of Financial Regulations* ruling the placement and adjudication of debt that contemplates the use of competitive bidding processes among financial institutions. Upon issuance of instruments, the main risk is associated with changes in inflation that affect bonds issued in UF.

Monitored market risk indicators include the term and currency of notes issued. Tables 5.2 and 5.3 show such indicators.

TABLE 5.2
STRUCTURE AND RISK OF THE DEBT PORTFOLIO OF CENTRAL BANK OF CHILE AS OF 31 DECEMBER 2017

Instrument	Ch$ million	UF%	Holding period (months)
Short-term	5,100,724.8	-	0.8
Long-term	9,735,959.0	62.3	52.2
Total	14,836,683.8	40.9	35.1

Source: BCCh.

TABLE 5.3
STRUCTURE AND RISK OF THE DEBT PORTFOLIO OF CENTRAL BANK OF CHILE AS OF 31 DECEMBER 2016.

Instrument	Ch$ million	UF %	Holding period (months)
Short-term	4,206,282.1	-	0.7
Long-term	10,907,860.2	62.9	57.2
Total	15,114,142.3	45.4	42.3

Source: BCCh.

(b) Credit risk

Credit risk is the risk of potential losses due to a counterparty failing to make a payment. The main source of risk arises from the investments in international reserves in debt instruments issued by foreign countries and financial institutions. A second source of credit risk comes from open market transactions and facilities that provide liquidity to the domestic financial system (Repo, FLI and FPL).

For international investments, the credit risk is mitigated by controls and limits established in the investment policies considering limits by type of risk (Sovereign, Supranational, Agencies and Banking), by type of instrument, issuer and counterparty, risk management of brokers and custodians. Additionally, the Company considers restrictions and controls by credit ranking related to the issuer of the instrument, which is calculated using the average ratings obtained from Fitch, Moody's, Standard and Poor's and DBRS; if only two ratings are available, the lowest will prevail; and in the event of only one rating is available, such rating will be used.

Tables 5.4 and 5.5 show the breakdown of reserves by credit rating and type of risk.

TABLE 5.4
BREAKDOWN OF THE INVESTMENT PORTFOLIO ACCORDING TO CREDIT RISK AS OF 31 DECEMBER 2017.

Credit Rating	Type of credit risk%				
	Agency	Banking	Sovereign	International	Total
AAA	0.8	0.0	80.5	3.1	84.4
AA+, AA, AA-	0.0	1.0	7.2	0.0	8.2
A+, A, A-	0.0	1.3	4.4	0.0	5.7
BBB+	0.0	0.0	1.7	0.0	1.7
Total	**0.8**	**2.3**	**93.8**	**3.1**	**100.0**

Source: BCCh.

TABLE 5.5
BREAKDOWN OF THE INVESTMENT PORTFOLIO ACCORDING TO CREDIT RISK AS OF 31 DECEMBER 2016.

Credit Rating	Type of credit risk %				
	Agency	Banking	Sovereign	International	Total
AAA	0.1	0.7	78.8	4.6	84.2
AA+, AA, AA-	0.0	1.2	9.3	0.0	10.5
A+, A, A-	0.0	2.5	1.9	0.0	4.4
BBB+	0.0	0.0	0.9	0.0	0.9
Total	**0.1**	**4.4**	**90.9**	**4.6**	**100.0**

Source: BCCh.

Credit risk associated with open-market transactions and facilities that inject liquidity into the local financial system (Repo, FLI, FPL) is mitigated by requiring collaterals eligible according to their credit quality, which are valued at market prices at the time of their receipt and subject to the application of discounts or haircuts according to the instrument specific characteristics.

As of 31 December 2017, the Bank recorded Permanent Liquidity Facility (FPL) operations of Ch$140,817.2 million and Repurchase Agreements (Repo) transactions for the injection of liquidity Ch$162,124.8 million. The average amount for 2017 was Ch$9,065.3 million for FPL and Ch$448.7 million for Repo, both collateralized through instruments issued by Central Bank of Chile and the General Treasury.

Tables 5.6 and 5.7 show the credit risk exposures related to the open-market transactions and facilities. We can identify that such risk is mitigated by the required collaterals, where Central Bank of Chile and General Treasury's securities are eligible.

TABLE 5.6
AVERAGE EXPOSURE OF FPL DURING 2017 AND 2016.

	Amount (Ch$ million)	
	2017	2016
Gross exposure	9,065.3	10,611.0
Collaterals:		
PDBC	(3,507.6)	(776.6)
BCCh bonds	(5,205.6)	(10,184.9)
BTP Bonds	(486.2)	-
Net exposure	**(134.1)**	**(350.5)**

Source: BCCh.

TABLE 5.7
AVERAGE EXPOSURE OF REPO TRANSACTIONS DURING 2017 AND 2016.

	Amount (Ch$ million)	
	2017	2016
Gross exposure	448.7	-
Collaterals:		
PDBC	(1.1)	-
BCCh bonds	(442.3)	-
BTP Bonds	(10.8)	-
Net exposure	**(5.5)**	**-**

Source: BCCh.

Additionally, at the end of December 2017, the Bank recorded swap purchase transactions in U.S. dollars associated with extraordinary actions for flexibilizing liquidity management of monetary market in foreign currency communicated by Central Bank of Chile on 15 December. Such program is transitional and a term of four weeks from its announcement.

Table 5.8 shows the credit risk exposures associated with the swap purchase transactions. Note that such risk is mitigated through the guarantees required.

TABLE 5.8
AVERAGE EXPOSURE OF SWAP DURING 2017 AND 2016.

	Average amounts	
	2017	2016
Gross exposure (US$ thousand)	82.2	-
Collateral:		-
Cash (Ch$ million)	(51.2)	-

Source: BCCh.

(c) Liquidity risk

Liquidity risk is the risk of not being able to settle an instrument or incurring losses when it is necessary to sell it due to a lack of market depth.

To reduce liquidity risk of the international reserves, a portfolio is mainly structured comprising fixed income securities traded in secondary markets of high liquidity and depth, and to a lesser extent short-term deposits in international commercial banks, with different due dates. The most liquid tranche includes instruments from the United States and Germany, as well as, overnight and weekend transactions, representing 67.9% of the internal investment portfolio in 2017 and a 62.3% in 2016.

For open-market transactions, this risk relates to the possibility of issuing bonds and promissory notes or rolling them over in the primary market at prices that are too high compared to securities with similar characteristics traded in the secondary market. This type of risk is mitigated through the provisions in current legislation contained in the *Compendium of Financial Regulations* that governs the placement and adjudication of debt and by monitoring both secondary and primary markets and their institutions. In the event of a decrease in demand for its securities, the Central Bank of Chile could pay its maturities by issuing cash.

For further information on maturities for Central Bank of Chile financial liabilities, see note 19 to these Financial Statements.

Tables 5.9 and 5.10 show a summary of the results of the granting of bonds and promissory notes for 2017 and 2016.

TABLE 5.9
RESULTS OF THE BIDDING OF DEBT INSTRUMENTS OF CENTRAL BANK OF CHILE AS OF 31 DECEMBER 2017.

Instrument	Amount granted in Ch$ million	Demand %	Award %	Bidding rate %	Market rate %	Spread (bp)
PDBC	53,770,000.0	150.4	99.9%	2.69	2.72	(3.0)
BCP	-	-	-	-	-	-

Source: BCCh.

TABLE 5.10
RESULTS OF THE BIDDING OF DEBT INSTRUMENTS OF CENTRAL BANK OF CHILE AS OF 31 DECEMBER 2016

Instrument	Amount granted in Ch$ million	Demand %	Award %	Bidding rate %	Market rate %	Spread (bp)
PDBC	36,550,000.0	146.2	101.4	3.47	3.55	(8.0)
BCP	800,000.0	144.6	75.0	3.89	3.88	1.0

Source: BCCh.

(d) Operational risk related to the financial instrument management

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events that prevent the normal performance of processes related to the financial instrument management.

The internal organization in Central Bank of Chile enables for an appropriate implementation of the design of processes related to financial instruments management, considering segregation of duties and responsibilities.

Consequently, the International Investments Management and Domestic Market Management with the Operations and Payment Systems Management, which report to the Financial Markets Division, are responsible for making investments and their settlement, respectively. The Financial Risk Management and Evaluation Management, reporting to the General Management, is responsible for issuing the performance and financial risks and ensure the compliance with investment limits.

Each management involved in the processes related to the financial instrument management, manages and controls its own operational risks. However, the Strategy and Operating Risk Management supports the divisions in the identification, analysis, evaluation and treatment of risks through a methodology that measures the inherent risk based on it feasibility and impact, and in the assessment of the residual risk we measure the effectiveness of the corresponding controls, in order to reduce the impact and/or possibility of occurrence. In addition, we track the action plans related to the risk management system and the business continuity system, including the results arising from the regular tests performed to ensure that the mechanisms developed to face contingency situations are working properly.

Central Bank of Chile Controllership, which reports directly to the Board, reviews regulatory compliance, the existence of an appropriate internal control environment and security of the information technology applications and infrastructure, as well as several issues related to governance, risks management, information and communication.

In addition, there are computer applications operating with market quality standards and we carried out initiatives to improve operational continuity, maintaining an alternate operation site to ensure the operation in case of problems with the physical infrastructure of the building and an external processing site in case of eventual technological failures which could affect its main technological processing site. The aforementioned elements ensure that the decision making and management evaluation process within Central Bank of Chile are appropriately defined.

Note 6
CASH AND CASH EQUIVALENTS

The detail of balances under cash and cash equivalents and their reconciliation to the statement of cash flows at each year-end is as follows:

	2017 Ch$ million	2016 Ch$ million
Correspondent banks abroad	721,350.1	683,756.5
Other reserve assets (foreign currency)	528.4	931.8
Domestic correspondents (*)	137.2	176.8
Total cash and cash equivalents	722,015.7	684,865.1

(*) These are included in the caption "Other securities" in the Statement of Financial Position

Note 7
NET INCOME FROM INTERNATIONAL RESERVES

(a) Foreign reserves

For the years ended 31 December 2017 and 2016, this caption is composed of the following:

	2017 Ch$ million	2016 Ch$ million
Net interests and commissions on:		
Securities recorded at fair value through profit or loss	257,732.8	275,424.2
Held-to-maturity securities	44,450.3	31,922.3
Held-for-sale securities	2,677.4	1,894.0
Foreign correspondents	6,714.1	3,367.9
Sub-total for net interest and commissions	311,574.6	312,608.4
Sales of securities:		
Recorded at fair value through profit or loss	(95,031.4)	(47,549.1)
Available for sale	22,702.2	12,108.4
Sub-total for sales of securities	(72,329.2)	(35,440.7)
Fair value adjustments:		
Gains from fair value adjustments	47,846.8	8,041.3
Losses from fair value adjustments	(111,296.1)	(68,879.2)
Sub-total for fair value adjustments	(63,449.3)	(60,837.9)
On other income	(121.0)	(2,613.2)
Total net income from international reserves	175,675.1	213,716.6

(b) Other foreign transactions

Net gain or loss on foreign transactions comprise the following:

	2017 Ch$ million	2016 Ch$ million
Revaluation of accounts with international agencies	8,395.8	39,128.9
Interest	(3,760.8)	(614.0)
Adjustment of amount of Fund for Special Operations, IDB	(32,312.6)	-
Other net income and expenses	(990.4)	(1,126.0)
Total net results from other foreign transactions	(28,668.0)	37,388.9

In accordance with Resolution AG-9/16 issued by the Inter-American Development Bank's Board of Governors, starting from 1 January 2017, Special Operations Fund (SOF) assets and liabilities were transferred to the Inter-American Development Bank's share capital under "Additional Capital Payable". For Central Bank of Chile, such transfer resulted in an impairment of the asset "Additional Capital Payable" of Ch$32.3126 billion equivalent to US$52.5 million.

Note 8
NET GAIN FROM DOMESTIC TRANSACTIONS

For the years ended 31 December 2017 and 2016, this caption is composed of the following:

	2017 Ch$ million	2016 Ch$ million
Income from domestic loans:		
Interest	581.2	744.9
Adjustments	(274.7)	(333.6)
Other income	4,545.9	7,773.6
Total income from domestic loans	4,852.4	8,184.9
Income from transactions under specific legal regulations		
Interest	13,497.5	19,518.0
Adjustments	9,915.4	18,841.4
Total income from transactions under specific legal regulations	23,412.9	38,359.4
Income from deposits and obligations held by Central Bank of Chile		
Interest	(63,743.9)	(94,357.4)
Other income	(281.9)	(412.6)
Total income from deposits and obligations held by Central Bank of Chile	(64,025.8)	(94,770.0)
Income from notes issued by Central Bank of Chile		
Interest	(515,407.5)	(529,455.1)
Adjustments	(106,462.3)	(196,748.2)
Total income from notes issued by Central Bank of Chile	(621,869.8)	(726,203.3)
Total net income from domestic transactions	(657,630.3)	(774,429.0)

Note 9
NET GAIN (LOSS) FROM FOREIGN EXCHANGE TRANSACTIONS

For the years ended 31 December 2017 and 2016, this caption is composed of the following:

	2017 Ch$ million	2016 Ch$ million
Gain on foreign exchange transactions	2,142,968.7	2,354,367.4
Loss on foreign exchange transactions	(3,120,348.6)	(3,977,541.5)
Total	(977,379.9)	(1,623,174.1)

Net gain (loss) from foreign exchange transactions for each year end, resulting mainly from the effect of exchange rate differences on foreign currency assets, as follows:

	2017 Ch$ million	2016 Ch$ million
U.S. dollar	(1,149,912.0)	(865,207.0)
Euro	196,637.2	(377,503.7)
Yuan	(9,433.7)	(67,670.0)
Canadian dollar	(7,376.6)	(34,209.4)
Korean won	23,797.7	(55,330.1)
Other currencies	(34,834.8)	(217,765.3)
Sub-total net (loss) gain from foreign exchange transactions	(981,122.2)	(1,617,685.5)
Arbitrage and other	3,742.3	(5,488.6)
Total net (loss) gain from foreign exchange transactions	(977,379.9)	(1,623,174.1)

Note 10
ISSUANCE AND DISTRIBUTION COSTS

For the years ended 31 December 2017 and 2016, this caption is composed of the following:

	2017 Ch$ million	2016 Ch$ million
Banknotes	(12,792.3)	(9,727.7)
Coins	(20,747.7)	(14,741.0)
Distribution	(1,585.1)	(1,685.5)
Total	(35,125.1)	(26,154.2)

Note 11
RESERVE ASSETS AND FAIR VALUES

(a) Reserve assets

This caption includes international reserves held by Central Bank of Chile and is detailed as follows:

	2017 Ch$ million	2016 Ch$ million
Monetary gold	6,305.8	6,070.8
Special drawing rights (SDR)	473,891.0	485,453.8
Reserve position in the International Monetary Fund (IMF)	154,491.6	143,497.2
Correspondent banks abroad	721,350.1	683,756.5
Investments	22,625,028.3	25,691,282.3
Securities recorded at fair value through profit or loss:		
Level 1 market value	19,569,596.6	18,322,931.3
Held-for-sale securities:		
Level 1 market value	1,492,666.8	3,085,235.9
Held-to-maturity securities	1,562,764.9	4,283,115.1
Reciprocal loan agreements	1,296.8	10,014.5
Other assets	528.4	931.8
Total reserve assets	23,982,892.0	27,021,006.9

	2017 US$ million	2016 US$ million
Monetary gold	10.2	9.1
Special drawing rights (SDR)	770.3	727.5
Reserve position in the International Monetary Fund (IMF)	251.1	215.0
Correspondent banks abroad	1,172.5	1,024.7
Investments	36,775.5	38,501.0
Securities recorded at fair value through profit or loss: Level 1 market value	31,809.1	27,458.8
Held-for-sale securities:		
Level 1 market value	2,426.2	4,623.5
Held-to-maturity securities	2,540.2	6,418.7
Reciprocal loan agreements	2.1	15.0
Other assets	0.9	1.4
Total reserve assets	38,982.6	40,493.7

As of 31 December 2017, monetary gold amounted to US$10.2 million (US$9.1 million in 2016) equivalent to 7,940 fine gold troy ounces valued at US$1,291.0 per ounce (US$1,145.9 in 2016). There was no change in the amount of troy ounces compared to 2016.

As of 31 December 2017 and 2016, the distribution of investments in foreign currencies by currency is as follows:

	2017 Ch$ million	2016 Ch$ million
U.S. dollar	15,481,136.5	18,456,296.0
Euro	3,588,688.5	3,662,447.3
Other	4,913,067.0	4,902,263.6
Total	23,982,892.0	27,021,006.9

	2017 Ch$ million	2016 Ch$ million
U.S. dollar	25,163.6	27,658.6
Euro	5,833.2	5,488.5
Other	7,985.8	7,346.6
Total	38,982.6	40,493.7

(b) Detail by type of assets of investments in foreign currency

	2017 Ch$ million	2016 Ch$ million
Securities at fair value through profit or loss		
Internal management portfolio:		
Bonds and nominal paper	14,639,859.9	15,695,833.8
Discounted commercial paper	3,703,470.4	1,938,301.7
Inflation-indexed bonds	587,453.5	54,818.1
Medium-term bonds issued by the BIS	6,126.4	-
Other assets	733.0	313.7
Sub-total	18,937,643.2	7,689,267.3
External management portfolio		
BlackRock external manager investments	321,715.8	321,802.9
Amundi external manager investments	310,134.1	311,773.2
Other assets	103.5	87.9
Sub-total	631,953.4	633,664.0
Total	19,569,596.6	18,322,931.3

	2017 Ch$ million	2016 Ch$ million
Available for sale investment securities		
Internal management portfolio		
Commercial paper	1,427,364.1	2,480,339.9
Short-term investments at fixed rate with the BIS	-	538,649.2
Collective investments through the BIS (BISIP)	65,302.7	66,246.8
Total	1,492,666.8	3,085,235.9

	2017 Ch$ million	2016 Ch$ million
Investment securities held to maturity		
Internal management portfolio:		
Term deposits	1,562,764.9	4,283,115.1
Total	1,562,764.9	4,283,115.1
Total investments in foreign currency	22,625,028.3	25,691,282.3

(c) Fair Values as of 31 December

Statement of Financial Position BCCh (Ch$ million)		2017			2016		
		Carrying amount (a)	Fair value (b)	Difference (b-a)	Carrying amount (a)	Fair value (b)	Difference (b-a)
Assets	International reserves	23,982,892.0	23,982,892.0	-	27,021,006.9	27,021,006.9	-
	Other foreign assets	117,796.4	117,796.4	-	160,574.2	160,574.2	-
	Loans to banks and financial institutions	302,947.8	302,947.8	-	12,501.8	12,501.8	-
	General Treasury transfers (Law 18,401)	305,069.6	227,047.6	(78,022.0)	299,945.0	231,814.5	(68,130.5)
	Subordinated liabilities (Laws 18,401 and 19,396)	231,291.0	236,597.1	5,306.1	355,006.0	367,254.4	12,248.4
	Other assets	57,835.4	57,835.4	-	58,970.5	58,970.5	-
	Total Assets	**24,997,832.2**	**24,925,116.3**	**(72,715.9)**	**27,908,004.4**	**27,852,122.3**	**(55,882.1)**
Liabilities	Monetary base	11,105,786.6	11,105,786.6	-	10,342,493.8	10,342,493.8	-
	Other deposits and obligations	3,728,419.1	3,728,419.1	-	5,061,911.8	5,061,911.8	-
	Obligations with General Treasury	317,897.9	317,897.9	-	780,412.4	780,412.4	-
	Notes issued by Banco Central Bank of Chile	14,836,683.8	15,330,456.3	493,772.5	15,114,142.3	15,893,661.4	779,519.1
	Foreign liabilities	768,875.8	768,875.8	-	790,794.1	790,794.1	-
	Other liabilities	23,505.5	23,505.5	-	24,131.6	24,131.6	-
	Total Liabilities	**30,781,168.7**	**31,274,941.2**	**493,772.5**	**32,113,886.0**	**32,893,405.1**	**779,519.1**
Equity	**Net equity**	**(5,783,336.5)**	**(6,349,824.9)**	**(566,488.4)**	**(4,205,881.6)**	**(5,041,282.8)**	**(835,401.2)**

Central Bank of Chile determines the fair value of the assets and liabilities for which a difference exists between their carrying amount and their fair value as follows:

- General Treasury transfers

Such amounts are derived from the provisions of Law 18,401 of 1985 and its amendments, and Law 18.577 of 1986 by way of which Central Bank of Chile sold to Corfo loan portfolios granted to financial institutions for the latter to finance the acquisition, by third parties, of shares of such financial institutions. In accordance with Article 13 of Law 18,401, the differences generated from the recovery as a result of the discounts granted to the shareholders, would be covered by the Chilean General Treasury through future General Treasury transfers of up to UF15 million.

By Executive Decree 1526 of 2010 the Ministry of Finance determined that the total amount of the transfer that the General Treasury has to perform in favor of Central Bank of Chile is equivalent to UF11.4 million and it has been established that such General Treasury transfer will be performed in annual consecutive payments, equivalent to, at least, one twentieth of the aforementioned total sum, starting on the eleventh year subsequent to the year in which the aforementioned decree was processed, which corresponds to 25 January 2011.

Fair value is determined on the basis of the present value of the annual payments indicated in such decree. BCU-30 market rates have been considered for the estimation of the present value of the payments.

- Cash receipts for subordinated obligation with financial institutions

This is generated by Law 18,401 of 1985 because of the financial crisis at the beginning of such decade. Such Law, specifically in Article 15, establishes that banks could substitute agreements pending the repurchase of portfolio with Central Bank of Chile, because of the new subordinated obligation, which in practice had an indefinite payment period.

In 1995, Law 19,396 established supplementing the previous law incorporating a maximum term of 40 years for the payment of the debt in partial payments, which are determined in accordance with the profits obtained by banks, defining a minimum payment, fixed payment, annual payment, "surplus for future deficit" account and annual 5% interest on the balance of the debt.

Through the present date, only *Banco de Chile* has subordinated obligation of Ch$231,291.0 million at the end of December, equivalent to UF8,630,858.4981 The subordinated obligation of *Banco de Chile* is secured by 28,593,701,789 shares of such bank through *Sociedad Administradora de Obligación Subordinada S.A. (SAOS)*, which at the end of September 2017 are equivalent to 28.75% of total shares of *Banco de Chile*.

The annual payment of the subordinated obligation has been made considering the net profits of *Banco de Chile* that can be distributed and ownership interest that Central Bank of Chile has through such guarantee. Despite the fact that a minimum payment of UF3.2 million has been established, the average annual payment for the last 5 years has been over UF5.0 million and as such under a conservative scenario, the final payment of the obligation would be made in 2019.

For the fair value estimation, an increase of 5% in the level of net distributable profits of *Banco de Chile* is used as scenario, considering the maintenance of the ownership interest that Central Bank of Chile has as pledge in such institution and in the discount of its cash flows at market rates bonds in UF of *Banco Chile* with a period similar to the estimated term of the obligation.

- Notes issued

The debt portfolio of Central Bank of Chile has been valued using a tool developed by the Bank based on zero-coupon yield curves in Chilean pesos and UF derived from market prices using the Svensson and Nelson-Siegel adjustment methods.

Note 12
RESERVE POSITION IN THE INTERNATIONAL MONETARY FUND (IMF)

The reserve position balance in the IMF at each year-end is detailed as follows:

	2017 Ch$ million	2016 Ch$ million
Subscription installment, contribution	1,528,280.0	1,564,744.5
New Arrangement to Borrow (NAB)	67,026.5	108,680.5
Deposits (Account No, 1 and 2)	(1,440,814.9)	(1,529,927.8)
Total position in the IMF	154,491.6	143,497.2

Note 13
LOANS TO BANKS AND FINANCIAL INSTITUTIONS

This caption includes the following transactions, which are defined as non-derivative financial instruments held-to-maturity, valued at amortized cost through the effective rate:

	2017 Ch$ million	2016 Ch$ million
Line of credit on debt restructuring	5.7	11.0
Central Bank of Chile repurchase agreements (Repo)	302,942.1	12,490.8
Total	302,947.8	12,501.8

Note 14
TRANSACTIONS UNDER SPECIFIC LEGAL REGULATIONS

This caption mainly includes the following transactions from specific laws that are defined as non-derivative financial instruments held to maturity, valued at amortized cost recognized in profit or loss through the effective rate.

(a) General Treasury transfers

The item "Tax transfers" under the specific legal regulation in the caption Transactions includes the following amounts:

	2017 Ch$ million	2016 Ch$ million
General Treasury transfer Law 18,401	305,069.6	299,945.0

In accordance with Article 13 of Law 18,401, differences produced in the recovery, as a result of discounts granted to shareholders of up to UF15.0 million, will be covered by the General Treasury through future transfers which as of 31 December 2017 amount to Ch$305,069.6 million, equivalent to approximately UF11.4 million (Ch$299,945.0 million in 2016, equivalent to UF11.4 million).

Executive Decree 1526 issued by the Ministry of Finance in 2010, determined the total amount of the transfer that the General Treasury has to perform in favor of Central Bank of Chile because of the application of the above mentioned law for UF11,383,983.4695 in annual installments equivalent, at least, to one twentieth of the aforementioned total sum, starting on the eleventh year subsequent to the year in which the aforementioned decree was processed, which corresponds to 25 January 2011. However, this decree expressly contemplates that the General Treasury will be able to make prepayments.

(b) *Caja Central de Ahorros y Préstamos* and *Asociación Nacional de Ahorro y Préstamo*

Through Decree Laws 1381 of 1976 and 2824 of 1979 the obligation imposed by Central Bank of Chile of granting loans to organizations which were part of the former National Savings and Loan System (Sinap) was regulated, because of the financial position affecting organizations in that system.

Central Bank of Chile granted the mentioned loans with a charge to its own resources through credit facilities for refinancing to organizations which were part of Sinap. In addition, the former *Caja Nacional de Ahorros y Préstamos*, part of Sinap, was also granted loans by the Chilean Government, with charge to the external resources from the Credit Program Agreement "AID 513–HG–006" entered into by the Republic of Chile, and applied through the Central Bank of Chile, as Fiscal Agent and Financial Agent, in accordance with Decree 20 of the Finance Ministry of 1976.

Subsequently, through Law 18,900 *Caja Central de Ahorros y Préstamos (CCAP)* and *Asociación Nacional de Ahorro y Préstamo (ANAP)* ceased to exist and a procedure was established through which the respective equity would be liquidated and used to pay shareholders and the obligations of the institutions.

Article 3 of the law establishes that *Caja Central de Ahorros y Préstamos* shall cease its transactions and with consideration of existing commitment, whether it has settled the liquidations required by the law or not, and shall include an inventory of all its rights, obligations and equity and those of the *Asociación de Ahorro y Préstamo*. This account will be submitted to the review of the President of the Republic through the Ministry of Finance. This article also stipulates the President of the Republic will approve such account through executive decree issued by the Ministry of Finance published in the *Official Gazette*.

Likewise, Article 5 of the aforementioned law establishes that the General Treasury shall be responsible for any obligations of the Sinap that are not covered upon liquidating shareholders' equity, the funds for which should be requested from the national budget, in conformity with Article 21 of Decree Law 1263 dated 1975.

The recovery of such amounts depends on the determination of a specific date for the payment of that loans, from the General Treasury in favor of Central Bank of Chile, which is not possible to determine because the Ministry of Finance has not issued the Decree approving the account for the *Caja* and the *Asociación*.

Accordingly, based on considerations solely for accounting and financial reporting purposes, as provided in Sections 18 No.9 and 75 et seq. of the Basic Constitutional Act regulating the Central Bank of Chile, the criteria and standards on International Financial Reporting Standards (IFRS), the Bank has determined that starting from year-end 2014 this Institution's financial statements will recognize an allowance for its losses in equity of Central Bank of Chile for the total amount of debt owed to the Bank by the entities comprising Sinap which are indefinitely in the process of liquidation.

Likewise, the obligation by the General Treasury established in Law 18,900, which guarantees the obligations of the abovementioned entities which could not be covered by the amount resulting from their liquidation, as indicated in several opportunities by the Ministry of Finance, is subject to the legal budget and the publication in the *Official Gazette* of the executive decree approving the liquidation account for such entities, because this had not yet occurred or has a determined verification date; the Central Bank of Chile has opted to reflect this situation in the notes to the financial statements to comply with the requirement of substantiating the rationale behind these decisions. Additionally, expressly indicate that the information contained in the preceding paragraph will only affect the method for recognizing the "Sinap liquidation Law 18.900" loan for reporting purposes, in accordance with IFRS standards. Accordingly, this should not and cannot be deemed, in any case, as a waiver by Central Bank of Chile of its right to continue to require the total and full payment of such debt.

Prior to making the decision mentioned above, the Bank informed the Minister of Finance. In response, the Minister responded the Bank that even though the President of Chile will approve such account through an executive decree issued by the Ministry of Finance, such approval has not been formalized because the requirement established by law for such purpose has not been met. In addition, the Minister indicated that because of this situation the Ministry of Finance was unable to express any opinion with respect to the balances in such account but acknowledged the information provided by the Bank.

Additionally, in relation to the part of the debt of the former *Caja Nacional de Ahorros y Préstamos* assumed by such entity in accordance with Decree 20 of the Ministry of Finance of 1976, considering that: (i) this transaction refers to an obligation in which the Central Bank of Chile was Fiscal Agent and Financial Agent of the General Treasury and (ii) once the condition established in Article 5 of Law18,900 has been complied with, the General Treasury will have the double status of creditor and debtor of such obligation. During this year, the Central Bank of Chile has determined that it is not applicable to recognize such part of the debt of the former *Caja Nacional de Ahorros y Préstamos* in its financial statements, and therefore, it derecognized such item from the Bank's asset and liability account. But whilst the mentioned condition is not verified, it will be registered at its adjusted value off balance-sheet accounts, under the name and on behalf of the General Treasury, for identification purposes, in order to distinguish it clearly from the higher part of the debt of the former Sinap corresponding to such other part financed directly by the Bank using its own resources, adjusting also the impairment recognized as of 31 December 2014.

In this respect, as of 31 December 2017, the amount owed by Central Bank of Chile for the settlement of the institutions that were part of Sinap, for the concept of credit facilities for refinancing granted directly to them charged to the Bank's own resources, amounts to Ch$1,211,447.4 million (Ch$1,134,052 million in 2016), included the impairment mentioned above. In addition, the updated value of the debt of the former *Caja Nacional de Ahorros y Préstamos*, member of Sinap, corresponding to the loans to related parties financed by the Chilean Government, through Central Bank of Chile, in accordance with Decree 20 stated above, amounts to Ch$84,702.3 million (Ch$81,702.0 million in 2016), which has been recognized in order accounts maintained by the Bank acting as Fiscal Agent of Chile.

(c) Loan for subordinated liability

The balances as of each year-end represent a subordinated liability of *Banco de Chile* with Central Bank of Chile as established in the agreement amending payment terms dated 8 November 1996, in accordance with the provisions of Law 19,396.

On that date, the parent company *Sociedad Matriz del Banco de Chile*, previously referred to as *Banco de Chile*, agreed to transfer the liability to *SAOS S.A.* (*Sociedad Administradora de la Obligación Subordinada*), based on paragraphs three and five of the aforementioned law. Consequently, the liability must be paid in 40 annual, consecutive and equal installments beginning in April 1997.

During 2017, *Sociedad Administradora de la Obligación Subordinada SAOS S.A.* paid UF5,344,803.0896 to Central Bank of Chile, of which UF660,655.2422 were allocated to the payment of interests of the debt and UF4,684,147.8474 to the credit amortization for subordinated liability (during 2016, a payment of UF5,426,250.9493 was made, from which UF897,552.1146 was destined to the payment of interest, and UF4,528,698.8348 to the repayment of principal owed).

As of 31 December 2017, the balance amounts to Ch$231,291.0 million, equivalent to UF8,630,858.4981 (Ch$355,006.0 million in 2016, equivalent to UF13,473.9114).

Note 15
PROPERTY, EQUIPMENT AND INTANGIBLE ASSETS

	2017 Ch$ million	2016 Ch$ million
Property and equipment, net	40,073.5	39,246.3
Intangible assets, net	3,003.8	2,359.3
Total property, equipment and intangible assets	43,077.3	41,605.6

(a) Reconciliation of property, equipment and intangible assets carrying amounts

This caption is mainly composed of the following balances and movements:

	(Ch$ million)					
	Balance as of 31. Dec. 16	Acquisi-tions	Dispo-sals	Depre-ciation	Transfers	Balance as of 31. Dec. 17
Real estate and facilities	27,696.3	29.6	-	(260.8)	-	27,465.1
Furniture and equipment	6,031.2	1,312.4	(37.3)	(1,625.1)	61.1	5,742.3
Transport material	220.8	56.3	(11.6)	(53.4)	-	212.1
Collection of banknotes and coins (*)	3,517.1	119.4	-	-	-	3,636.5
Works of art	1,645.4	-	-	-	-	1,645.4
Work in progress	135.5	1,297.7	-	-	(61.1)	1,372.1
Net property, plant and equipment	39,246.3	2,815.4	(48.9)	(1,939.3)	-	40,073.5

(*) Variation of $119.4 million is due to variations in foreign currency exchange of gold peso.

As of 31 December 2017 and 2016, the caption Depreciation and Amortization in the statement of income includes Ch$1,939.3 million and Ch$2,611.1 million, respectively.

(b) Reconciliation of Intangible Assets carrying amounts

Composition and movements of intangible assets

	Ch$ million				
	Balance as of 31. Dec.16	Acquisi-tions	Amortiza-tion	Transfers	Balance as of 31. Dec. 17
Computer programs	2,238.8	1,177.1	(814.7)	-	2,601.2
Computer programs under development	120.5	282.1	-	-	402.6
Intangible assets, net	2,359.3	1,459.2	(814.7)	-	3,003.8

As of 31 December 2017 and 2016, the amortization of intangible assets of Ch$814.7 million and Ch$822.3 million is recorded on a straight-line basis in the caption depreciation and amortization in the statement of income.

(c) Operating lease contracts

As of 31 December 2017 and 2016, there are no non-cancellable operating lease contracts.

Note 16
FOREIGN LIABILITIES

This caption includes the following transactions:

		2017 Ch$ million	2016 Ch$ million
Reciprocal loan agreements	16 a	41.7	49.9
Accounts with international organizations	16 b	52,250.6	57,681.3
Special drawing rights (SDR) allocations	16 c	716,583.5	733,062.9
Total foreign liabilities		768,875.8	790,794.1

16.a Reciprocal Loan Agreements (credits) represent the amount owed by Central Bank of Chile to the central banks comprising Aladi's Agreements on Reciprocal Payments and Credits for the imports conducted by Chilean entities. Its classification corresponds to non-derivative held-to-maturity securities, valued at amortized cost at effective rate.

16.b Accounts with international organizations correspond to resources held in local currency by such organizations for its drawing and to obligations of Central Bank of Chile acting as a Fiscal Agent, with IDB, for promissory notes subscribed in foreign currency in payment of the subscription of shares and capital increases. They do not bear interest, but maintain their value for the fluctuations in the United States dollar.

This caption is composed of the following:

	2017 Ch$ million	2016 Ch$ million
Promissory note obligations with IDB	49,119.8	53,277.2
Inter-American Development Bank (IDB)	2,187.9	3,445.9
Agency for International Development (AID)	901.1	901.1
Multilateral Investment Guarantee Agency (MIGA)	32.9	32.9
International Bank for Reconstruction and Development (IBRD)	8.9	24.2
Total accounts with international organizations	52,250.6	57,681.3

16.c The assignments of Special Drawing Rights (SDRs) correspond to SDR817,868,312 assigned to Chile through Central Bank of Chile, by the International Monetary Fund, which are subject to possible restitution; they accrue interests on the basis of a rate determined by the IMF on a weekly basis.

Note 17
MONETARY BASE

This caption is composed of the following:

	2017 Ch$ million	2016 Ch$ million
Banknotes and coins in circulation	8,970,283.8	8,651,831.2
Deposits from financial institutions	1,527,426.8	1,690,662.6
Deposits for technical reserve	608,076.0	-
Total monetary base	11,105,786.6	10,342,493.8

(a) Banknotes and coins in circulation

Includes the amount of banknotes and coins of legal tender issued by Central Bank of Chile held by third parties, resulting from the total banknotes and coins received from suppliers and recorded as liabilities at their face value, less the banknotes and coins that are in the cash of Central Bank of Chile and in its vaults.

Banknotes and coins in circulation are recorded at face value. The costs of printing and coining are recorded as expense in the caption issuance and distribution costs.

The distribution of banknotes and coins in circulation as of 31 December of each year is as follows:

Bank notes denomination	2017 Ch$ million	2016 Ch$ million
$ 20,000	4,236,709.3	3,820,699.0
$ 10,000	3,578,742.9	3,720,204.8
$ 5,000	344,462.3	349,155.5
$ 2,000	79,090.4	74,930.9
$ 1,000	280,348.3	267,264.1
$ 500	4,716.9	4,742.2
Various	251.4	251.4
Total	8,524,321.5	8,237,247.9

Coins denomination	2017 Ch$ million	2016 Ch$ million
$ 10,000	348.4	348.4
$ 2,000	98.6	98.6
$ 500	201,382.5	183,695.2
$ 100	148,086.2	139,910.4
$ 50	28,133.9	26,183.4
$ 10	52,261.7	48,699.2
$ 5	10,852.9	10,847.1
$ 1	4,726.0	4,728.9
Other	72.1	72.1
Total	445,962.3	414,583.3

(b) Deposits from financial institutions

Deposits from financial institutions reflect the movements in drafts and deposits in local currency resulting from transactions performed by financial institutions with Central Bank of Chile. Their balance represents the funds or reserves in favor of financial institutions and is used for the constitution of cash positions.

(c) Deposits for technical reserve

This refers to compliance with the obligation on the technical reserve contemplated for banking entities in Article 65 of the General Banking Law, which establishes the alternative of maintaining deposits with Central Bank of Chile for such purposes. Such legal precept provides that deposits in current account and other deposits and on demand deposits, which a bank receives, as well as the amounts that has to destine to pay on demand obligations which it assumes within its financial line of business, to the extent that they exceed two times and a half their effective equity, should be maintained in cash or in a technical reserve consisting of deposits with Central Bank of Chile or in notes issued by the General Treasury at any term valued at market price.

Note 18
DEPOSITS AND OBLIGATIONS

Deposits and obligations correspond to financial liabilities, classified as held to maturity for deposits held in Central Bank of Chile, by the General Treasury, as well as by financial institutions and are composed of the following:

	2017 Ch$ million	2016 Ch$ million
Deposits and obligations with General Treasury	317,897.9	780,412.4
Other deposits and obligations	3,728,419.1	5,061,911.8
Total	4,046,317.0	5,842,324.2

(a) Deposits and obligations with the General Treasury include:

	2017 Ch$ million	2016 Ch$ million
General Treasury current accounts	317,897.9	780,412.4
Total	317,897.9	780,412.4

Other Deposits and Obligations include:

	2017 Ch$ million	2016 Ch$ million
Permanent Deposit Facility in local currency	2,258,529.4	1,380,669.1
Current accounts in foreign currencies	415,544.3	1,124,993.3
Short-term deposits from bank institutions in foreign currencies	1,021,265.2	2,532,365.6
Other	33,080.2	23,883.8
Total	3,728,419.1	5,061,911.8

Note 19
NOTES ISSUED BY CENTRAL BANK OF CHILE

The issuance of notes by Central Bank of Chile is the main element supporting the implementation of the monetary and debt policy in order to provide liquidity to the market and deepen its transactions in an efficient manner. These financial liabilities are classified as held-to-maturity and valued at amortized cost using the effective interest method.

As of 31 December 2017 and 2016, maturities of these instruments are as follows:

	(Ch$ million)						
	Up to 90 days	91 - 180 days	181 days to one year	More than one year to 3 years	Over 3 years	Total 2017	Total 2016
Central Bank of Chile bonds in UF (BCU)	978,624.6	-	822,948.1	25,748.3	4,169,639.3	5,996,960.3	6,777,119.7
Central Bank of Chile bonds in Chilean pesos (BCP)	252,094.3	329,273.7	-	1,981,499.4	1,106,615.0	3,669,482.4	4,037,484.6
Central Bank of Chile discountable promissory notes (PDBC)	4,977,255.5	64,371.4	58,866.6	-	-	5,100,493.5	4,206,282.1
Optional indexed coupons (CERO) in UF	8,834.4	1,955.5	10,349.2	27,737.9	2,244.4	51,121.4	66,314.1
Indexed promissory notes payable in coupons (PRC)	397.0	245.1	297.9	3,590.9	14,087.4	18,618.4	26,930.3
Other	7.8	-	-	-	-	7.8	11.5
Total as of 31 December	6,217,213.6	395,845.7	892,461.8	2,038,576.5	5,292,586.1	14,836,683.8	15,114,142.3

Balances include interest and adjustments accrued as of 31 December 2017 and 2016.

Note 20
PROVISIONS

Central Bank of Chile has recorded provisions for severance indemnity, a benefit established in the Collective Labor Agreement in force for the periods 2011-2015 and 2015-2019 accounted for in accordance with the actuarial method of projected cost. At the same time, the benefits granted to the former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile and healthcare benefits for retirement plans are also included and detailed as follows:

	2017 Ch$ million	2016 Ch$ million
Provisions for the year:		
Severance indemnity	12,749.3	12,259.7
Special indemnity and agreed deposit for retirement plan Resolution 1651	2,004.7	1,593.9
Sub-total provision for severance indemnity	14,754.0	13,853.6
Benefits to the former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile	2,305.1	2,448.9
Healthcare benefits for retirement plans	8.1	12.3
Pending accrued vacations of personnel	2,735.7	2,571.0
Special indemnity, Resolution 572-05-961226	1.1	1.1
Incentive allocation	364.1	316.9
Sub-total other provisions	5,414.1	5,350.2
Total	20,168.1	19,203.8

	2017 Ch$ million	2016 Ch$ million
Movements in provisions for severance indemnities (*):		
Current value of liabilities as of 1 January	13,853.7	13,022.2
Current value of service costs	1,262.2	1,275.0
Interest cost	640.0	586.0
Benefits paid	(835.1)	(532.2)
Actuarial gains (losses)	(166.8)	(497.4)
Total	14,754.0	13,853.6

(*) This does not include benefits for the Former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile, retirement health care plans and incentive payments.

	2017 Ch$ million	2016 Ch$ million
Post-employment benefit expenses		
Current value of service costs	1,154.5	1,156.4
Interest cost	753.7	701.6
Total	1,908.2	1,858.0

As of 31 December 2017, the sensitivity of the actuarial liability amount from post-employment benefits considering changes indicated in actuarial assumptions generates the following effects:

Calculation of variable sensitivity analysis impact	Base Scenario	Scenario 1	Scenario 2
Discount rate (%)	4.62	3.62	5.62
Effect on provisions for severance indemnity payments (Ch$ million)	14,753.9	16,063.6	13,643.1
Effect on provision for severance indemnity payments (%)	-	8.88	-7.53

Calculation of probable payment of the provision for severance indemnity payments	(Ch$ million)
Short-term provisions for severance indemnity payments (up to one year)	1,812.0
Long-term provisions for severance indemnity payments (over one year)	12,942.0
Balance as of 31 December	14,754.0

Note 21
CAPITAL AND RESERVES

(a) Capital and reserves

Section 5 of the Basic Constitutional Act of Central Bank of Chile established an initial capital for Central Bank of Chile at $500,000 million, which at 31 December 2017 corresponds to $2,482,447.9 million adjusted to the Consumer Price Index as of that date, with a time lag of one month, which has to be paid according to transitory Article 2 of the Basic Constitutional Act.

In accordance with Section 77 of the Basic Constitutional Act of Central Bank of Chile, the deficit produced in any year will be absorbed with a debit to constituted reserves.

When there are no, or insufficient, reserves, the deficit produced in any period will be absorbed with a debit to capital.

As of 31 December 2017, Central Bank of Chile has negative equity of Ch$5,783,336.5 million (negative equity of Ch$4,205,881.6 million as of 31 December 2016) arisen mainly from differences between international reserve returns and the cost of liabilities at domestic interest rate due to gains and losses from changes in the exchange rates of assets in foreign currencies.

(b) Price-level adjusted capital

The Board decided to no longer apply comprehensive price-level adjustment to financial statements beginning in 2010, and therefore price-level adjustment on capital is no longer presented in the statement of financial position nor in the statement of comprehensive income; however, in order to comply the provisions of Section 5 of the Basic Constitutional Act of Central Bank of Chile, paragraph 2, which states "The capital may be increased by decision of the majority of the Board Members, through capitalization of reserves and adjusted by means of price-level adjustment", as well as stated in Title VI of the same legislation, regarding the distribution of Central Bank of Chile surpluses included in Section 77, and the payment of the initial capital referred to in transitory Article 2. Once the initial capital, properly adjusted as stated in the terms of Section 5 is paid, the resulting surplus for each year, will be determined and calculated for the purposes of surplus distribution to the General Treasury as contained in Section 77, considering the annual adjustment to the equity recorded in memorandum accounts.

As of 31 December 2017, the negative capital price-level adjustment recognized in memorandum accounts amounted to a negative equity of Ch$94,967.2 million (negative equity of Ch$79,322.6 million in 2016), which resulted in adjusted capital at the reporting date of Ch$5,093,240.9 million (negative equity of Ch$2,814,584.5 million in 2016). The amount to price-level adjusted is capital at the reporting date which includes the capital adjusted at the prior year-end, plus the profit or loss from such year and its contributions by the General Treasury, if any, which does not consider valuation accounts. Note that as of to-date the related deficit has not been distributed yet and during 2017, there were no capital contributions by the General Treasury.

	Capital as of 31. Dec. 2017 before price-level adjustment	Price-level adjustment in memorandum accounts	Price-level adjusted total capital as of 31. Dec. 17
Balances as of 31 December 2017	(4,998,273.7) (*)	(94,967.2)	(5,093,240.9)

(*) Corresponds to price-level adjusted capital as of 31 December 2016 plus profit or loss for the same year.

Note 22
FOREIGN CURRENCY BALANCES

The statement of financial position includes assets and liabilities payable in foreign currencies, whose balances as of 31 December, 2017 and 2016 are as follows:

	2017 US$ million	2016 US$ million
Assets		
Foreign assets	39,174.1	40,734.4
Reserves	38,982.6	40,493.7
Other foreign assets	191.5	240.7
Other asset accounts	12.6	11.0
Total assets	39,186.7	40,745.4
Liabilities		
Foreign liabilities	1,244.7	1,178.5
Other foreign liabilities	79.9	79.9
Special drawing rights (SDR) allocations	1,164.8	1,098.6
Domestic liabilities	2,907.8	5,994.6
Deposits and obligations with General Treasury	516.7	474.2
Other deposits and obligations	2,391.1	5,520.4
Other liabilities	1.8	0.2
Total liabilities	4,154.3	7,173.3
Net assets	35,032.4	33,572.1

Note 23
CONTINGENCIES AND COMMITMENTS

There are no lawsuits that are in process against Central Bank of Chile; accordingly, the Bank has recorded no contingencies that are expected to have a material effect on equity.

Note 24
INCOME TAXES

Pursuant to Article 7 of Decree Law 3345 dated 1980, Central Bank of Chile is exempt from income taxes.

Note 25
FISCAL AGENCY

Law 20,128 related to General Treasury Liability created the "Economic and Social Stabilization Fund" (FEES) and the "Pension Reserve Fund" (FRP)". In conformity with the provisions of the aforementioned law, through Executive Decree 1383, dated 2006 of the Ministry of Finance amended Executive Decree 1618 dated 2012, and appointed Central Bank of Chile as Fiscal Agent for the administration of resources referred to such funds, in conformity with the procedures, conditions, methods and other standards established in the aforementioned decree.

Executive Decree 19 in 2011, issued by the Minister of Finance, appointed Central Bank of Chile as Fiscal Agent for the administration of the Strategic Contingency Fund.

In accordance with Article 5 of the abovementioned Executive Decree 1383, as amended by Executive Decree 1618, investments of public resources managed by Central Bank of Chile, as Fiscal Agent, have been carried out in accordance with the guidelines established for these effects by the Ministry of Finance. These investments have been recorded in off balance sheet accounts of Central Bank of Chile.

On 18 June 2015, via Resolution 1909-02, the current execution guidelines for the Pension Reserve Fund and the Economic and Social Stabilization Fund, respectively, were approved. On 18 July 2013, by Resolution 1765-04, the current execution guidelines for the Strategic Contingency Fund were approved.

Note 26
TRANSACTIONS WITH RELATED PARTIES

(a) Central Bank of Chile does not have any related companies.

(b) Compensation of the Board and key executives:

According to Central Bank of Chile Basic Constitutional Act, compensation of the Board is set by the President of the Republic for periods not exceeding two years, following a proposal made by a commission formed by former governors and deputy governors of the entity, appointed by the President of the Republic. In order to propose compensation, the act requires them to be based on the compensation paid to the highest-ranked executive positions in bank institutions within the private sector.

Compensation corresponding to the General Manager, the General Counsel and General Auditor of Banco Central de Chile, are at level one of the compensation structure, as they are positions established in Sections 24 through 26 of the Central Bank of Chile´s Basic Constitutional Act.

The total gross compensation paid to the Board and key executives during 2017 amounted to Ch$1,445.2 million (Ch$1,493.8 million in 2016).

Note 27
RELEVANT EVENTS

(a) On 6 December 2017, subsequent to complying his 10-year term, the Counselor and Deputy Governor of Central Bank of Chile Mr. Sebastián Claro Edwards left office.

(b) On 22 August 2017, by Resolution 2085E-01, the Board agreed to appoint Mr. Anthony Dawes Martindale as member of the Audit and Compliance Committee of Central Bank of Chile for a three-year term replacing Mr. Jesús Riveros Gutiérrez who ended his period.

Note 28
SUBSEQUENT EVENTS

In the opinion of Management, between 31 December 2017 and the date of issuance of these financial statements the following subsequent events which could significantly affect the amounts presented in the financial statements have occurred:

(a) Change in U.S. dollar and euro exchange rate.

The exchange rate for U.S. dollar as of 24 January 2018 amounted to Ch$608.15 representing a decrease of Ch$7.07 compared with the exchange rate prevailing as of 31 December 2017. This represents a decrease in Central Bank of Chile equity of Ch$157,238.0 million.

The exchange rate for Euro as of 24 January 2018 amounted to Ch$747.20 representing an increase of Ch$11.99 compared with the exchange rate prevailing as of 31 December 2017. This represents an improvement in Central Bank of Chile´s equity of Ch$59,007.2 million.

The total decrease in Central Bank of Chile equity because of the decrease in the exchange rate for United States dollar and Euro on 24 January 2018 amounts to Ch$98,230.8 million.

(b) Approval of financial statements

The financial statements for the year ended 31 December 2017 were presented by the General Manager to the Central Bank of Chile Board on 30 January 2018, and approved for issue at the Meeting Session 2127.

(c) Other

There are no subsequent events that might have a significant effect on the amounts presented herein or in Central Bank of Chile´s economic or financial position.

ALEJANDRO ZURBUCHEN SILVA
General Manager

JUAN CARLOS SALAZAR TAPIA
General Accountant

SILVIA QUINTARD FLEHAN
General Auditor

INDEPENDENT AUDITORS' REPORT

The Governor and Members of
Central Bank of Chile:

Report on the financial statements

We have audited the accompanying financial statements of Central Bank of Chile, which comprise the statements of financial position as of 31 December 2017 and 2016, and the related statements of comprehensive income, changes in equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards; this includes the design, implementation and maintenance of internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Generally Accepted Auditing Standards in Chile. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Central Bank of Chile as of 31 December, 2017 and 2016 and the results of its operations and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

The above translation of the auditors' report is provided as a free translation from the Spanish language original, which is the official and binding version. Such translation has been made solely for the convenience of non-Spanish readers.

Mario Torres S. KPMG Ltda.

Santiago, 30 January 2018

BANCO CENTRAL DE CHILE